

**Strategic Alliances; The Role of Central Firm in
Governing Strategic Alliances Between Small and
Medium Size Companies; The Case in the Icelandic
Fish Industry**

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I confirm that the thesis is my own work and I alone am responsible for the work carried out in order to produce the thesis.

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Abstract

This research was conducted on two marketing companies, the Icelandic Freezing Plant Corporation (IFPC, established 1942) and the Union of Icelandic Fish Producers (UIFP, established 1932) in the Icelandic Fish Industry, established by producers to export and market their products. The main research question is “*What is the role of the “central firm”¹ in strategic alliances involving large numbers of small and medium size enterprises*”? The main emphasis is on studying the governance of vertical alliances with a high number of participants’ companies. These two alliances have changed from being joint ventures owned by producers to market their products to becoming independent Limited Liability Companies on the public stock markets. The research is based on case study methods where each marketing company is taken as a separate case. Data was collected through various first and secondary data, such as interviews and archival sources. Conclusions were drawn from each case separately and then a mutual conclusion drawn from both cases.

It is argued in the research findings that the role of the central firm in governing alliances with a high number of participants’ companies should be threefold; a coordinator, a strategic leader and a creative environment for the participants’ companies. Two types of administrative mechanisms were identified, that is, a formal mechanism based on centralisation and an informal mechanism based on direct communication. It is suggested that the informal mechanism is much more likely to shape a value creative environment for the participants’ companies, while the formal mechanism was more economical in an environment where value creation was not required. In both cases, some mixture of these two mechanisms was used and in accordance with the demands of value creation.

¹ In this thesis the term “central firms” is used to refer to the company that has an intermediary role in strategic alliances and takes care of some joint activities for participants’ companies.

Contents

I	INTRODUCTION.....	1
I.1	PURPOSE AND AIMS OF THE STUDY.....	7
I.2	IMPLICATIONS OF THE STUDY	9
I.3	STRUCTURE AND SUMMARY OF CHAPTERS	10
II	RESEARCH METHODOLOGY	12
II.1	RESEARCH PERSPECTIVE	13
II.1.1	<i>Case studies.....</i>	<i>17</i>
II.1.2	<i>Grounded Theory.....</i>	<i>18</i>
II.2	SCOPE OF THE RESEARCH	21
II.3	DATA COLLECTION AND ANALYSIS	23
II.4	ETHICAL CONSIDERATIONS	26
II.5	LIMITATION TO THE STUDY.....	27
II.6	HUMAN PERCEPTIONS	28
III	BACKGROUND	30
III.1	GEOGRAPHY AND CLIMATE	30
III.2	NATURAL RESOURCES	31
III.3	HISTORY.....	31
III.4	DEMOGRAPHY AND CULTURE	32
III.5	ICELANDIC ECONOMY	33
III.5.1	<i>Gross Domestic Product.....</i>	<i>33</i>
III.5.2	<i>The Labour Market.....</i>	<i>34</i>
III.5.3	<i>Foreign Trade.....</i>	<i>37</i>
III.5.4	<i>Investment and Interest Rate.....</i>	<i>39</i>
III.5.5	<i>Inflation.....</i>	<i>41</i>
III.5.6	<i>Economic Policy in Iceland.....</i>	<i>42</i>
III.5.6.1	Minor Government Interference 1876-1930	42
III.5.6.2	Government Interference 1930-1960.....	43
III.5.6.3	Adjustment to International Business Environment 1960-1990.....	45
III.5.6.4	Open Economy 1990-1999	49
III.6	GOVERNMENT AND POLITICAL ENVIRONMENT	51
III.7	CONCLUSIONS	53
IV	THE ICELANDIC FISH INDUSTRY.....	56
IV.1	BRIEF HISTORY	56
IV.2	STRUCTURE AND DEVELOPMENT	57
IV.2.1	<i>Fishery Sector.....</i>	<i>59</i>
IV.2.1.1	Rowing boats 1750-1850.....	59
IV.2.1.2	Sail boats 1850-1905.....	59
IV.2.1.3	Motor boats and trawlers 1905 - 1945.....	59
IV.2.1.4	Innovation-trawlers and Swedish boats 1945 - 1970.....	60
IV.2.1.5	Stern-trawlers 1970 - 1985	61
IV.2.1.6	Processing-trawlers 1983 - 1997.....	61
IV.2.2	<i>Fish Farming.....</i>	<i>62</i>
IV.2.3	<i>Fisheries control and management.....</i>	<i>63</i>
IV.2.3.1	Icelandic economic exclusive zone	63
IV.2.3.2	The Quota system.....	64
IV.2.3.3	Individual transferable quota (ITQ).....	65
IV.2.4	<i>Fishing fleet and catch.....</i>	<i>68</i>
IV.2.5	<i>Processing Sector.....</i>	<i>70</i>
IV.2.5.1	Production methods.....	71
IV.2.5.1.1	Drying (Stockfish).....	72
IV.2.5.1.2	Salting.....	73
IV.2.5.1.3	Freezing.....	73
IV.2.5.1.4	Meal and oil.....	74

IV.2.5.1.5	Canning and preserving.....	75
IV.2.5.1.6	Fresh (Iced).....	75
IV.2.6	<i>Export Sector</i>	76
IV.2.6.1	Government interference and oligopoly 1930 - 1987.....	77
IV.2.6.2	Competition and increased freedom 1980 -1999.....	80
IV.2.6.3	Market developments.....	83
IV.2.7	<i>Profitability and Development of Companies</i>	85
IV.3	CONCLUSIONS.....	88
V	LITERATURE REVIEW.....	92
V.1	DEFINITIONS OF STRATEGIC ALLIANCES.....	93
V.1.1	<i>Types of Strategic Alliances</i>	96
V.1.2	<i>Characteristics of Strategic Alliances</i>	98
V.2	RATIONALISATION OF STRATEGIC ALLIANCES.....	102
V.2.1	<i>Value Chain and Strategic Positions of Companies</i>	104
V.2.2	<i>Strategic Contribution of Strategic Alliances</i>	108
V.3	NETWORK PERSPECTIVE.....	110
V.4	GOVERNANCE OF STRATEGIC ALLIANCES.....	115
V.4.1	<i>Administration mechanism</i>	116
V.4.1.1	Coordination.....	119
V.4.1.2	Strategic centre.....	122
V.4.2	<i>Organisational demands of Strategic alliances</i>	124
V.4.2.1	Culture.....	128
V.4.2.2	Trust and Attitude.....	130
V.4.2.3	Power.....	131
V.4.2.4	Uniqueness of SMEs.....	135
V.5	CONCLUSIONS.....	136
VI	RESEARCH FINDINGS.....	142
VI.1	UNION OF ICELANDIC FISH PRODUCERS.....	142
VI.1.1	<i>History and Development</i>	142
VI.1.1.1	Establishment and Entrepreneurship 1932 - 1957.....	143
VI.1.1.2	Monopoly 1957 - 1990.....	146
VI.1.1.3	Increased competition 1990 - 1993.....	150
VI.1.1.4	Transformation 1993 - 1998.....	154
VI.1.2	<i>Analysis of UIFP case</i>	158
VI.1.2.1	Forms and nature of the alliance.....	158
VI.1.2.1.1	Dependency of actors in the network.....	166
VI.1.2.1.2	Conflict of interest and value creation in the network.....	168
VI.1.2.2	Role of the central firm in the alliance.....	172
VI.1.2.3	Governance of the network.....	176
VI.1.2.3.1	Mechanism.....	176
VI.1.2.3.2	Power.....	179
VI.1.2.3.3	Strategy.....	180
VI.1.2.3.4	Social maturity and trust.....	182
VI.1.3	<i>Conclusion</i>	183
VI.2	ICELANDIC FREEZING PLANT CORPORATION.....	188
VI.2.1	<i>History and development</i>	188
VI.2.1.1	1942 - 1962 Establishment and Entrepreneurship.....	188
VI.2.1.2	1963 -1982 Growth and expansion.....	192
VI.2.1.3	1980 - 1985 Strategy- and Generation Changes.....	196
VI.2.1.4	1986 -1997 Globalisation and Structural Changes.....	199
VI.2.1.5	1997 - 1999 Independence.....	207
VI.2.1.6	1999 - ?.....	210
VI.2.2	<i>Analysis of the IFPC Case</i>	212
VI.2.2.1	Nature and forms of the alliance.....	212
VI.2.2.1.1	Nature of the alliance.....	216
VI.2.2.1.1.1	Stakeholders.....	217
VI.2.2.1.1.2	Dependency of actors in the alliance.....	218
VI.2.2.1.2	Conflict of interest.....	221

VI.2.2.2	Role of the central firm in the alliance	228
VI.2.2.3	Governance of the alliances.....	232
VI.2.2.3.1	Mechanism.....	232
VI.2.2.3.2	Power.....	240
VI.2.2.3.3	Strategy.....	245
VI.2.2.3.4	Knowledge, Communication and IT.....	249
VI.2.2.3.5	Social maturity and trust.....	252
VI.2.3	Conclusion	254
VII	CONCLUSION	263
VII.1	MUTUAL CONCLUSION AND COMPARISON.....	263
VII.1.1	<i>Form and Structure of the Alliances</i>	263
VII.1.2	<i>Governance of the Alliances</i>	268
VII.1.3	<i>Role of the Central Firm</i>	273
VII.2	THEORETICAL IMPLICATIONS.....	278
VII.3	IMPLICATIONS FOR THE ICELANDIC FISH INDUSTRY	283
VII.4	FURTHER RESEARCH	288
	BIBLIOGRAPHY	290

List of Figures

FIGURE II.1 THE SCOPE OF THE RESEARCH AND NUMBER OF COMPANIES.....	21
FIGURE III.1 GEOGRAPHIC DISTRIBUTION OF FOREIGN TRADE IN 1996.....	38
FIGURE III.2 COMPARISON OF INFLATION 1956 – 1996 (RATES AVERAGED OVER 5 YEARS).....	41
FIGURE III.3 INFLATION IN ICELAND 1955 – 1996 (YEAR-ON-YEAR RATE).....	41
FIGURE IV.1 MAIN FACTORS OF THE FISH INDUSTRY AND THEIR IMPACTS.....	57
FIGURE IV.2 PRODUCTION THE FISH PROCESSING 1975-1997	72
FIGURE IV.3 MARKETS FOR EXPORT OF FISH PRODUCT FROM ICELAND 1975 - 1995.....	81
FIGURE V.1 STRATEGIC ALLIANCES' OPTIONS BETWEEN THE PARENT FIRMS.....	94
FIGURE V.2 ARCHETYPES OF STRATEGIC ALLIANCES	96
FIGURE V.3 STRATEGIC ALLIANCES' OPTIONS IN TERMS OF DEGREE OF VERTICAL INTEGRATION	103
FIGURE V.4 THE FOUR MODES OF ORGANISING ECONOMIC ACTIVITIES.....	104
FIGURE V.5 BASIC STRUCTURAL MODEL OF NETWORK.....	112
FIGURE V.6 RELATIONS BETWEEN ACTORS AND ACTIVITIES/RESOURCES	117
FIGURE V.7 DIFFERENT FORM OF RELATIONS BETWEEN COMPANIES.....	121
FIGURE VI.1 MAIN FORM OF UIFP UNTIL 1993	158
FIGURE VI.2 FORM OF UIFP RELATIONSHIP WITH PRODUCERS FROM 1993 – 1999.....	161
FIGURE VI.3 UIFP STRUCTURE 1999-	162
FIGURE VI.4 NUMBER OF PRODUCERS AND PERCENT OF TOTAL SALE UIFP 1194 - 1998 ..	164
FIGURE VI.5 TOTAL SALE OF SH SPLIT AFTER MARKET AREAS 1943-1997.....	197
FIGURE VI.6 FORM OF THE IFPC ALLIANCES 1942 - 1962.....	212
FIGURE VI.7 FORM OF IFPC ALLIANCES 1963 - 1996	213
FIGURE VI.8 FORM OF IFPC ALLIANCES 1997 - 1999	214
FIGURE VI.9 FORM OF IFPC ALLIANCES 1999 - ?	215
FIGURE VI.10 TYPES OF INTERACTION IN IFPC NETWORK	239
FIGURE VII.1 NETWORK PERSPECTIVE	282

List of Tables

TABLE II.1 NUMBERS OF INTERLOCUTORS AND INTERVIEWS	22
TABLE III.1 CONTRIBUTION OF INDUSTRIAL SECTORS TOWARDS GDP	34
TABLE III.2 EMPLOYMENT BY INDUSTRIES	36
TABLE III.3 COMPOSITION OF COMMODITY EXPORTS	37
TABLE III.4 COMPOSITION OF COMMODITY IMPORTS	38
TABLE III.5 THE YEAR ICELAND JOINED INTERNATIONAL ORGANISATIONS	39
TABLE III.6 INVESTMENT BY SECTORS AND INDUSTRIES	40
TABLE III.7 AVERAGE REAL INTEREST RATE	40
TABLE III.8 AVERAGE ANNUAL INFLATION: GDP IMPLICIT PRICE INDEX	46
TABLE IV.1 PRODUCTION OF FISH FARMING 1992 - 1995	62
TABLE IV.2 THE FLEET, SIZE AND CATCH 1997.	68
TABLE IV.3 THE FLEET, MAIN SPECIES AND FISHING GEAR.	69
TABLE IV.4 TOTAL CATCHES 1997.	69
TABLE IV.5 TEN MOST IMPORTANT SPECIES IN FISH CATCH 1997.....	70
TABLE IV.6 PROFIT FROM REGULAR OPERATION AS A PERCENTAGE OF REVENUES 1980-1996..	86
TABLE IV.7 QUOTA OF THE TEN BIGGEST COMPANIES AS A PERCENTAGE OF ASSIGNED QUOTAS EACH YEAR.....	87
TABLE V.1 ALTERNATIVE BUSINESS RESPONSES TO THE GLOBAL MARKETPLACE.....	95
TABLE V.2 CATEGORY OF STRATEGIC ALLIANCES.	98
TABLE V.3 DEVELOPMENT OF COLLABORATION OF COMPANIES.....	101
TABLE V.4 BENEFITS FROM NEW SUPPLIERS' AND CUSTOMERS' APPROACH.....	108
TABLE V.5 STRATEGIC CONTRIBUTIONS OF JOINT VENTURES	109
TABLE V.6 COMPARISON OF THE OLD AND NEW APPROACH TO MANAGEMENT	127
TABLE V.7 DIFFERENCES BETWEEN LARGE AND SMALL COMPANIES.....	135
TABLE VI.1 CONSOLIDATED FINANCIAL KEY FIGURES.	157
TABLE VI.2 SHAREHOLDERS 01.06.99	163
TABLE VI.3 ACTORS, ACTIVITIES AND RESOURCES	165
TABLE VI.4 DEVELOPMENT OF MEMBERS AND OWNERSHIP IN IFPC	204
TABLE VI.5 KEY OPERATIONAL AND FINANCIAL FIGURES 1986 - 1996.....	207
TABLE VI.6 KEY OPERATIONAL AND FINANCIAL FIGURES 1997 - 1998.....	210
TABLE VI.7 ACTORS, ACTIVITIES AND RESOURCES	217

I Introduction

In business, the formation of alliances between companies in one form or another is inescapable. The most common form of alliance usually occurs where relationships between companies and their suppliers and customers are close. Other forms of alliances, such as joint ventures, licensing and networks of firms, are apparently becoming important in both domestic and international business¹. Cooperation and competition have often been put forward as a contrast. It is equally important, in companies' strategies, to be able to cooperate with other companies as well as compete with them². Examples of cooperation between companies include networks, inter-firm cooperation, cooperative strategy, joint venture, strategic networks, franchising, and licensing. Any arrangements in which companies agree *formally* to cooperate are increasingly called "strategic alliances". A strategic alliance is defined here as "*where two or more companies cooperate together to attain shared strategic objectives*³". This definition includes cooperative arrangements such as a joint venture, collaborative venture, licensing, franchising, subcontracting and suppliers' and customers' relationships that build on close cooperation in matters such as research and development (abbreviated R&D) and quality control.

The increasing speed of change in the business strategic environment of the past two decades makes it even more difficult for companies to focus entirely on a "going it alone" strategy⁴. Companies face hard and often unfamiliar competition from unexpected directions such as rival alliances. This makes the business environment even more unpredictable⁵. Today's business strategic environment involves rapid changes caused by increased global competition, faster technological changes and variations in customers' demands. These include:

¹ Alter, C. & Hage, J.

² Contractor, J. F. & Lorange, P.

³ This definition supports to definition that has been put forward by, Lorange P. & Roos J., page vi, 1993.

⁴ Contractor, J. F. & Lorange, P.; Harrigan, R. K. 1985.

⁵ Hayes, H. R. & Pisano, P. G.

- **Social:** For example changes in fashion, family size, as well as increased interest in health food and environmental issues which in turn lead to new consumption patterns and customer demands.
- **Political:** The opening up of new markets, for example China and even the temporary slowing down of others, as happened when the East-European bloc collapsed or during the 1998 economic problems in Asia.
- **Increased global competition** from companies in countries like Taiwan, South Korea and China.
- **Demands from customers.** Some aspects such as quality are now taken for granted so it is no longer a major competitive advantage as was true 10 - 15 years ago⁶.
- **Technological:** Where the technology is becoming more complicated causing some firms to emphasise their R&D investment.

It would be easy to carry on with this enumeration. Clearly, these changes in the business environment have caused senior managers and owners of companies to realise that they face difficulties coping with both old as well as new forms of competition. These problems push firms to examine close cooperation with other companies. The main motives for most alliances appear to be to gain access to knowledge and skills, and/or to lower costs, and/or to achieve the ability to overcome and/or heighten barriers for new entrants and/or sharing risk⁷. By forming alliances, companies can strengthen their own competitive stances by sticking to their core business and expertise while letting their partner companies with other appropriate resources take care of what they in turn do best.

Although turbulence in the business environment seems to have increased the importance of strategic alliances in some form or another, there is evidence to suggest that strategic alliances are not a straightforward strategic choice⁸. Cooperative arrangements between companies put great pressure on management to share information and values and possibly to integrate part of their activities. This is likely to be hard for companies that do not have the organisational ability to cope with such arrangements. This is especially true if the organisational structure of the participating companies is hierarchical and bureaucratic, causing them to be incapable of coping with the demands of co-operating closely with other companies⁹. Cross frontier

⁶ Hamel, G & Prahalad, K.C.

⁷ Dunning, H. J.; Alter, C. & Hage, J.

⁸ Parker, N.

⁹ Hasting, C.

partnerships between companies may face additional problems due to differences in value systems, labour practice, law, language and culture. Problems can also occur in collaboration between domestic companies. The reported high percentage of failures of strategic alliances demonstrates possible operating problems¹⁰. It has been pointed out that special abilities are required of managers in strategic alliances as opposed to those necessary for hierarchically structured firms pursuing a “go it alone strategy”¹¹.

Much of the literature on strategic alliances relates to either international joint ventures between two large companies of different nationalities¹² or, increasingly, to studies of close relationships between large companies and their suppliers¹³. Most of the published examples are of firms in the automobile industry in the US and Japan, or of firms in the aerospace industry. There is little discussion in the literature of alliances between domestic companies, although these are increasingly common in mature economies such as in the US and, of course, in Japan¹⁴. In addition there is little published research on strategic alliances between small and medium size companies particularly if the alliances involve ten or more participants¹⁵ (as in so called marketing cooperative). Small and medium size enterprises (abbreviated SMEs¹⁶) could be said to require alliances at least as much if not more than large companies. This is due to their resource constraint, which hinder the SMEs abilities to market internationally (as in this study), take on major projects and/or invest heavily in R&D. Hence, it can be argued that the competitive position of SMEs can be improved by their collaboration with other companies in a similar situation in some kind of alliance¹⁷.

¹⁰ Parker, N.

¹¹ Hasting, C.

¹² See for example Harrigan, R. K., 1985.

¹³ See for example Helper, S.; Human, E. S. & Provan, K.

¹⁴ Harrigan, R. K., 1985.

¹⁵ Human, E. S. & Provan, K.

¹⁶ In this thesis SMEs is defined as companies with 1 - 500 employees.

¹⁷ Alter, C. & Hage, J.

Due to differences in the nature of SMEs and large companies, the strategic alliances between SMEs could differ from what is known about strategic alliances between large companies. Differences in alliances between SMEs and between large companies may be due to limited resources resulting in a higher dependency by SMEs on the alliances than in the case for larger companies, the greater number of companies in each alliance may well require a different administration mechanism to that in alliance between a limited number of large companies, differences in the power structure due to a high level of dependency on the alliance, lower levels of resources and finally differences in aims and strategy of such cooperative alliances. These issues have not received much attention from academics, and there is therefore causing little understanding of the suggested difference in strategic alliances between SMEs and large companies.

The organisational form (structure) and the administrative mechanism of strategic alliances as a whole are said to be unstable. Such alliances can be seen as lying between two extremes. On the one hand there is the firm operating in a totally open “market” - an economic “free for all” in which the firm competes with all others to gain an advantage not only against direct competition but also in terms of other resources and market position. On the other hand there is the firm which attempts to gain market control over the input-output situation through vertical integration (“hierarchy”)¹⁸. Researchers have increasingly emphasised that strategic alliances should not be viewed as some kind of intermediate position on a single dimensional scale between “market” and “hierarchy” but as a unique type¹⁹. This leads to a discussion on the mechanism needed to govern strategic alliances where there is neither the hierarchy-controlled process of a vertically integrated firm nor the “invisible hand” of the market ruled by price and other competitive activities²⁰. Academics in the organisational field are not unanimous about the mechanism and methods to govern the alliances. On the one hand are those that look at this process almost as a “grassroots

¹⁸ Lorange, P. & Roos, J., 1993 based on transaction cost theory by Williamson, 1975.

¹⁹ Axelsson, B.

²⁰ Axelsson, B.

mechanism” that uses very informal methods from coordination²¹. On the other hand are the advocates of using a more formal mechanism to co-ordinate activities and resource in the alliances²². Clearly, internal organisational relationships as in strategic alliances, demand the existence of some kind of administrative mechanism²³ to permit the sharing of information and knowledge as well as to co-ordinate activities²⁴. This is crucial if the strategic alliance is to be efficient and competitive. Academics have pointed out that more research is required focusing on the long-term development of such alliances and methods of management to support a better understanding of the way they operate²⁵. This debate about the administrative mechanism is very relevant for alliances between SMEs due to the often high number of participants and limited resources, suggesting different patterns to those in alliances or networks between large companies.

As has been described, strategic alliances of all types between SMEs have not received much attention from academic researchers despite their apparent strategic value to SMEs. This indicates a gap in the study of strategic alliances. The intention of this research is to contribute to filling this gap by studying three marketing companies in the Icelandic fish industry established by groups of small processing companies to take charge of the export of their products. The three marketing companies established by producers (who process fish caught by their own fishing vessels or by other individual fishing vessels) that was originally planed to studied here are; the Sölusamband Íslenskra Fiskframleiðenda (Union of Icelandic Fish producers) abbreviated UIFP, established 1932, Sölumiðstöð Hraðfrystihúsanna (Icelandic Freezing Plants), abbreviated IFPC, established 1942 and Íslenskar Sjóvarafurðir (ÍS/SÍS) (Icelandic Seafood/Federation of Icelandic Co-operatives) abbreviated IS. These three companies have had the dominant share of the export of fish products from Iceland; in 1982 these three companies exported 71.5% of the total fish

²¹ Thompson, P. & McHugh, D.

²² Thompson, P. & McHugh, D.

²³ Axelsson, B.

²⁴ Johnston, R. & Lawrence, R. P.

²⁵ Axelsson, B.

products²⁶. Due to increased freedom permitted by the government of Iceland in the export of fish, which led to increased competition, this proportion has fallen to 57.0% in 1991²⁷.

At around the same time as this research began (1995/96), Icelandic Seafood faced increased operational difficulties, leading to financial problems of Icelandic Seafood. This can be traced to high investment at the same time that the company was facing poor profitability and the collapse of a big project in Russia. These problems led to Icelandic Seafood denying the author access to its companies concerning this research, thereby reducing the number of marketing companies in the study to two. Icelandic Seafood and Icelandic Freezing Plant were very similar companies and both specialised in selling frozen fish. Historically, Icelandic Freezing Plant have had a 50% higher portion of the export of frozen fish from Iceland than Icelandic Seafood. The development and structure of Icelandic Freezing Plants and Icelandic Seafood have in many cases been similar, so it can be argued that no important or different information about alliances between the marketing companies and their producers will be left out by omitting Icelandic Seafood.

Over 95% of all fish products from Iceland are exported so the processing companies have depended, for their financial viability, on the export of their products and therefore on the success of their alliances. IFPC was originally established by privately owned processing companies but UIFP was established by processing companies that were both privately owned as well as in cooperative ownership. Both IFPC and UIFP operated on co-operative bases until 1992 when UIFP was changed into a limited liability company and later, in 1996, IFPC went through the same changes. Until the ownership changes of these two companies, they both operated as marketing co-operative organisations, which returned their profits to their members through taking a lower commission on sales of fish. Since the formation of the two marketing co-operatives the nature of the alliances has changed due to the drive by the marketing co-operatives' concerns to become

²⁶ Bjarnason, A.

²⁷ Bjarnason, A.

independent. The study of these two marketing companies provides an excellent opportunity to study the development and nature of such (marketing cooperative) strategic alliances between SMEs. The objectives of the proposed study include:

- Analysing the governance of strategic alliances between high numbers of small and medium size enterprises and the role of “central firm” in the governance and structure of such alliances.
- Analysing alliances with a “large” number of participants and the impact the number of actors has on the strategy of the alliances.
- Analysing the development of the two alliances over a 50 years period and the changes in the aims and forms of these alliances during that period.
- Analysing two exporting companies operating in a rather homogenous strategic environment, which appear to have developed distinctive strategies.

1.1 Purpose and Aims of the Study

The main purpose of this research is to study the historic development of the “central firm”²⁸ in strategic alliances between large groups of SMEs, in order to provide a better understanding of such alliances. The nature of this research is explanatory and descriptive, with the emphasis on analysing what are the key factors in the development of the “central firm” and its transition into an independent company in the Icelandic fish industry. The goal is to increase understanding about this development and generate some knowledge emerging from the empirical part of the study in order to contribute to the identified gap in the literature (see chapter V).

The main research question therefore is:

“What is the role of the “central firm” in strategic alliances involving large numbers of small and medium size enterprises?

- a) What is the role of the central firm in the governance (administrative mechanism/coordination/management) of the alliances?*
- b) What methods have been used to co-ordinate activities and actors in the alliances as a whole?*
- c) How has the structure of the alliances changed over the operation time and what has influenced these changes?”*

The research will cover the history of the two strategic alliances in the Icelandic fish industry from their beginning until today (1998). In these alliances the “central firm” is the intermediary between the producers and the international process and/or retail distribution end of the supply chain and is therefore responsible for all marketing activities outside Iceland. The main emphasis in this research will be on the development of the “central firm” but it is considered necessary to study the complete chain of processes from the producers to the market, in order to develop a more holistic picture of these alliances, their developments and the inter-connection of the key factors found in the study.

Specific topics, which emerged from the general purpose and the main research objectives, are:

- I. The role of the two marketing companies as “central firm” in the alliances, stressing over several levels in the value adding chain.
- II. The role of the central firm in the “governance” of the alliances as a whole and what impact changes have on the administrative mechanism of the alliances.
- III. The structure of the strategic alliances and how these have evolved and developed.
- IV. Finally, the academic literature in strategic alliances will be compared with the findings of this research.

From the research questions as well as the nature of the research it should be clear that this study is aimed at the managerial aspect of strategic alliances between small and medium size companies. As has been pointed out this aspect of strategic alliances between SMEs has received little attention from academics, leaving a gap in the literature. Research on strategic alliances has in many cases focused on the economical aspect of companies working together with the main focus on explaining the reasons for their existence and different forms of such arrangements. Rather than taking this economical view of the strategic alliances, this research will focus on the managerial aspect of operating such an inter-relationship between companies. Academics have increasingly pointed out that a better

²⁸ In this thesis the phrase “central firm” is used to refer to the company that has an intermediary role in strategic alliances and takes care of some joint activities for participant companies.

understanding is needed of the methods of management of strategic alliances and other forms of inter-organisational relationship²⁹.

1.2 Implications of the study

Implications of this research are threefold. Firstly it will contribute to the theories about strategic alliances, secondly it will contribute to business policy of small and medium size companies, and thirdly it will benefit companies in the Icelandic fish industry.

First of all, this research is meant to contribute to the increased body of knowledge and theories of companies' relationships and, more specifically, of strategic alliances between small and medium size companies. Due to little research and even lack of knowledge of the managerial aspect of strategic alliances, and even more so in alliances between small and medium size enterprise, an attempt will be made to help fill that gap with this research. In that way it will contribute to theories of networking and strategic alliances by adding to them a research on long term alliances in the Icelandic fish industry providing an excellent opportunity to study long term changes on such alliances. This research will also draw out the difference between alliances of large companies and SMEs by comparing the academic literature of strategic alliances with the findings of the empirical research that will be undertaken in this study. Hence, the research will more clearly establish what this difference includes, which will be of great relevance for further research in this field.

Secondly, this research is aimed at contributing to the business policy of small and medium size companies by studying the long-term alliances between such companies in the Icelandic fish industry. Lessons will be drawn from the two alliances that could contribute to other SMEs by adding knowledge to the management of strategic alliances, which involve a high number of participants. This is important for the strategy of small and medium size companies, which often have to look for extension of their business through alliances with other companies due to lack of resources (for example, capital and human resources).

²⁹ Obsborn, N. R. & Hagedoorn, J.; Axelsson, B.; Alter, C & Hage, J..

Thirdly, it is inevitable that this research will also contribute to the Icelandic fish industry due to the fact that the two companies that are studied are all operating in that business. Better understanding of the managerial aspect of the alliances that the majority of companies in the Icelandic fish industry are participating in, will inevitably contribute to the industry and therefore the Icelandic economy as a whole.

The fact that only two companies are studied and both in the same business and country limits the generalisation of the study, however it makes comparison more reliable than if the companies would have been from different industries or countries.

1.3 Structure and summary of chapters

This thesis is divided into 7 chapters. Chapter II is the research methodology chapter providing an overview of the research methods used in this research. In this research, multiple sources of data are used such as archival data, articles, annual reports, companies' newsletters and histories of the two companies. In addition to this, interviews were used as a main source of data in studying the last period of the development of the companies. The main research method is case studies where the two cases are taken as separate cases and then mutual conclusions are drawn. Chapter III provides basic information for the background of the study, that is, geographical and economical information about Iceland. This chapter shows the importance of the Icelandic fish industry for the Icelandic economy and for the local communities that the industry is operating in. Chapter IV describes the Icelandic Fish Industry, its development and characteristics. This chapter shows that great changes have occurred in the fish industry since the quota system was implemented in 1983. The main characteristics of these changes are concentration of the companies in the industry. Four main factors are indicated as main factors in these changes. These four factors are the quota system, increased freedom in export of fish products in Iceland, increased freedom in the Icelandic economy and finally increased entrance of companies in the fish industry into the public stock market. Chapter V provides the critical Literature review concerning

cooperation between companies. The main emphasis is on strategic alliances, as well as on the growing literature about networking of companies. In chapter VI the cases of Union of Icelandic Fish Producers and Icelandic Freezing Plants are presented. This chapter is divided into two subchapters one for each case. Discussion about each case is split into three parts: First, the analytical view over the history and development of the company is presented. Secondly, more analytical analysis is presented of the development of these networks. This analysis is built upon the archival sources although the main emphasis is on data taken from the interviews. The third and last part includes conclusions for each case. The last chapter in this thesis presents the conclusions and implications of this work, where the main findings from the empirical study are drawn together, and comparisons are made between the two cases as well as with existing literature. Finally the implications of this study for the Icelandic fish industry and the Icelandic economy are presented along with a discussion of theoretical implications and suggestion for further research.

II Research Methodology

As stated in the introduction, the original idea of this research was to study three of the big marketing companies in the Icelandic fish industry. The accessibility to the companies limited this down to two companies, IFPC and UIFP. The third company that was originally to be included in this research, Icelandic Seafood, was going through great difficulties during the time the research was undertaken. These difficulties were reflected by great changes inside Icelandic Seafood such as changes on the management team, which could have made research on them difficult. Due to these difficulties, Icelandic Seafood denied the author access to the company for this research. Later, in autumn 1999, Icelandic Seafood merged with UIFP. The development of Icelandic Seafood and IFPC through the history of the two companies has been almost identical. Both companies have been selling their products on the same markets with a similar strategy of operating sales offices and secondary processing plants in the market area. The relationship with the producers has more or less developed in the same way, where producers were the owners and dominated the boards of the two companies. The development of Icelandic Seafood is explained in chapter IV which deals with the Icelandic fish industry. Some lessons were also drawn from the development of Icelandic Seafood and these are included in chapter VI in relation to research findings. It is therefore claimed that the absence of Icelandic Seafood in the research will not leave out important data for this project.

The fourth primary marketing company that would have been possible to include in this research was the Icelandic Herring Board. The Icelandic Herring board is in many ways different from the other primary marketing companies in that it was not established by producers to sell their products, but was much more a governmental institution where the parliament and the Ministry of Fishery nominate members of board. The Icelandic Herring board had a monopoly on the export of Herring from Iceland for a long time. This direct governmental influence differs greatly from the other three marketing companies that were established by producers for producers so Icelandic Herring Board is therefore not included in this research. The

Icelandic Herring Board was in 1998 changed into a Limited Liability Company and renamed Íslandssíld hf., which in 1999 merged with UIFP. Hence, during the period of this research, UIFP has merged with two of the three remaining marketing companies, leaving only UIFP and IFPC of the four that would have been a possible sample in the beginning of this research.

II.1 Research Perspective

The main aim of this research is to analyse the role of the central firm in the governance of strategic alliances between high numbers of SMEs companies. The focus is on the governance of the network, and on what has influenced it and changed it over the operation time of the alliances. The main research question is therefore:

“What is the role of the “central firm” in strategic alliances involving large numbers of small and medium size enterprises?

- a) What is the role of the central firm in the governance (administrative mechanism/coordination/management) of the alliances?*
- b) What methods have been used to co-ordinate activities and actors in the alliances as a whole?*
- c) How has the structure of the alliances changed over the operation time and what has influenced these changes?”*

The objective of the research is to provide an analysis on the development of these two networks, in order to generate knowledge that will contribute to the identified gap in the literature about networking between small and medium size companies (see chapter V).

Human and Provan point out that there are very limited comparative empirical studies on SMEs networks and that it is difficult to make generalisations about them because most the research relates to large companies¹. Other academics have pointed out the need for a multidimensional perspective in studying strategic alliances and networks. Osborn and Hagedoorn for example *“encourage researchers to abandon a singular, clear-cut description of alliances and networks based on the*

¹ Human, E. S. & Provan, K.

assumption of a host discipline in favour of a more robust, sophisticated, multidimensional vision"². In a similar way Easton points out that in such a young paradigm as network research *"there exists a remarkable number of alternative views and perspective, sometimes espoused by the same author at different times. In addition since these are views of the same phenomena from different angles they are irreconcilable and cannot be integrated..."*³. According to these there is not much to build on to make comparable research or to use a known methodology from other studies, especially in connection to SMEs, as is the case here.

Another factor that influenced the choice of research methodology for this study is the importance of the Icelandic fish industry for the Icelandic economy in general, in particular, for those individual areas whose prosperity is built upon the operation of the fish industry. In the past, this has often been reflected in great social pressure on companies in the industry leading to business decisions that are not the most efficient or profitable. With increased competition and pressure from owners (shareholders) of the companies, profit and efficiency plays a bigger role in the decision making process today than in the past. This social pressure, as well as the number of owners, conflict of interest and the mixed form of relationships makes the decision of what research framework to use in studying this development rather difficult. Nohria points this out when he claims that in studying organisation it has been too common that the environment is treated as a black box⁴. According to Nohria it is important to recognise the environment and its impact on the companies⁵. Due to this it is clear that it would be difficult to use the traditional "dominant perspective", such as the competitive analysis of Porter where outside companies are viewed as "extended rivals"⁶ and the transactional cost theories that focus on the single relationship that a company has with its

² Osborn, N. R. & Hagedoorn, J., page 274.

³ Easton, G., page 4.

⁴ Nohria, N.

⁵ Nohria, N.

⁶ Johnston, R. & Lawrence, R. P.

suppliers or customers⁷. In addition to this there is only a very limited body of research on the business environment in the Icelandic fish industry or the operation of companies in the industry⁸. It is therefore the author's conclusion that it is necessary in researching strategic alliances to view the participating companies as a part of the network and embedded in the environment that it is working in, and not as a single free standing unit. This can be supported by Easton where he claims that *"if strong relationships exist among buyers and sellers then the facile switching among easily available alternatives which is assumed in economic analysis no longer applies"*⁹. Furthermore he claims that history becomes important and *"the rules of optimum resource allocation fail as relational constraints start to bite and motives other than short term profit maximisation begin to dominate"*¹⁰. Hence it seems clear that a mixture of frameworks is needed where both efficiency and social factors are acknowledged as pressures or reasons for decision-making. This is supported by the increased interest in using mixed framework in organization research¹¹. Perhaps this trend also reflects a growing disappointment with theories that portray efficiency as the driving force behind decision-making¹².

As has been presented, the objective of this research is to study the role of the central firm as well as the structure and governance of strategic alliances in the Icelandic fish industry. Barley and Tolbert point out that *"researcher(s) who wish to study changes in institutions that govern the action of collective activities may therefore need to resort to historical and archival data. Studies of inter-organisational networks suggest that researchers can reconstruct relationships among organisations over time by drawing on a variety of archival sources"*¹³. This supports the argument that the research methods need to be connected to historical analysis of

⁷ Axelsson, B.; Alter, C. & Hage, J.; Osborn, N. R. & Hagedoorn, J.

⁸ See for example Bjarnason, A.

⁹ Easton, G., page 6.

¹⁰ Easton, G., page 6.

¹¹ Clegg, R. S.

¹² Clegg, R. S.

¹³ Barley, R. S. & Tolbert, S. P., page 105.

various data in this research. It is not enough to use a single method of data collection, but rather various sources such as archival analyses and interviews. This also emphasises the need for research to stretch over a longer period to get better understanding and a more holistic picture of the development in the organisation and the driving forces for the institutional changes.

The network perspective offers an opportunity to adopt both the economical as well as the social aspects in the research framework, and is therefore a good starting point in network research. Although the network perspective is a good starting point the actual research methods must also be suitable for the use of variable sources, including both secondary and archival data as well as primary data such as interviews. In the critical literature review chapter (chapter V) it is pointed out that further research is needed on the governance on the strategic alliances¹⁴. Due to the lack of a pre-existing body of theory about governing of strategic alliances the nature of this research is explanatory, aiming at increasing understanding and generating some knowledge emerging from the empirical part of the study. This research will be based on a broad range of data sources that are both historic and contemporary, as well as data collection from interviews and documentation. Hence, the research methods must be able to deal with these various sources and methods. Hamel and Fortin claims that case studies employ various research methods and data sources¹⁵. In a similar way Bryman claims that “*case studies can and do exhibit the whole gamut of methods of data collection*”¹⁶. Bryman carries on by claiming that one case can involve a number of different methods, both quantitative and qualitative, within a single case¹⁷. Hence, having considered the theoretical aspect of the research as well as the fact that the research is dealing with two central firms and their strategic alliances, case study methods have been chosen as the main approach to study this research topic.

¹⁴ See for example, Osborn, N. R. & Hagedoorn, J.; Axelsson, B.; Alter, C. & Hage, J.

¹⁵ Hamel, J. D. & Fortin, D.

¹⁶ Bryman, A., page 172.

¹⁷ Bryman, A.

II.1.1 Case studies

Yin claims, *“that a case study arises from the desire to understand complex social phenomena and is a flexible and widely used method”*¹⁸. He also defines case studies as an *“empirical inquiry, within a real-life context where the boundaries between phenomena and context are blurred and using multiple source of evidence”*¹⁹. Robson gives a similar definition that a *“case study is a strategy for doing research that involves an empirical investigation of a practically contemporary phenomenon within its real life context using multiple sources of evidence”*²⁰. One of the academics’ concerns is whether the case study is a method or an approach. Hamel, Dufous and Fortin claim, *“case studies employ various methods. These can include interviews, participant observation, and field studies. Their goals are to reconstruct and analyse a case from a sociological perspective. It would thus be more appropriate to define the case study as an approach, although the term case method suggest that it is indeed method”*²¹. From this it can be seen that the case studies approach can combine various research methods, which is very helpful in studying the two marketing companies and their relationship with producers with over fifty years’ history and the various data that the research will be based on. Hence, it is the author’s conclusion to use case studies in conducting this research.

In studying the relationship between the marketing companies and their producers in the Icelandic fish industry it turned out that very limited research has been done on that phenomena, or indeed on the Icelandic fish industry at all. This means that the present study cannot build on a body on research on the companies in the fish industry. Hence, this research needs to build up an understanding of the marketing companies and their relationship with their producers. It is the author’s conclusion that use of quantitative research methods on phenomena with limited previous knowledge and research to build upon would not be trustworthy enough.

¹⁸ Yin, K. R., page 14.

¹⁹ Yin, K. R., page 14.

²⁰ Robson, C., page 5.

²¹ Hamel, J., Dufour, S. & Fortin, D., 1991.

Hence, by applying only quantitative methods such as survey, there is a danger that the research would not reflect the most important aspect of the relationship and therefore miss out vital information due to lack of pre-understanding of the phenomena. It is the author's conclusion that to be able to conduct analytical research on the network, a qualitative research approach is needed where the emphasis is to give a holistic and an analytical view on the network.

Each case will be analysed on its own, and conclusions will be drawn from each one. In addition to that, mutual conclusions will be drawn from the two cases, where they will be compared to each other as well as being evaluated against the theoretical framework provided in the literature review chapter. Using two sets of data or two cases makes demands on the data collection to ensure that it is comparable data across the cases²². In this research this is in many ways given by the fact that both of the marketing companies are in the same business in the same country. It is clear though that the nature of their operation is not quite the same due to different numbers of producers inside each network and differences in the product range of the two companies. To ensure that the data collection based on interviews will be reasonably comparable, semi-structured interviews will be used to guarantee that the same topics are covered. Other options would have been to use more standardised closed questions but it was the author's conclusion that due to the lack of existing research about the networks that would not provide the same depth to the data collection as having the interlocutors expressing their thoughts in their own language.

II.1.2 Grounded Theory

Data collection in this research is based on multiple sources, as has been discussed, although interviews play a big part. The case studies do not provide a method for analysing data; rather they provide a framework to host other methods of data collection and analysis. It is the author's conclusion that it is necessary to bring in a more structured way of collecting and analysing data for the two cases. Hence, methods of

²² Bryman, A.

grounded theory were used as a “guideline” in the data collection for this research. Grounded theory is a method of analysing various sources of data such as non-standardised text, transcripts or other kinds of qualitative data²³. Grounded theory was developed initially in the 1960s by two sociologists, Barney Glaser and Anselm Strauss. Although both sociologists, they came from different backgrounds. Glaser was trained in quantitative research methods whereas Strauss was strongly influenced by what has come to be known as the Chicago School of thought - the University of Chicago has a long history of pioneering and innovating qualitative research approaches²⁴. The methodology of grounded theory was conceived in an attempt to develop scientific respectability for qualitative research.

In grounded theory data are collected through observations in the field, interviews with participants, diaries and other documents like letters or even newspapers. Data are initially coded with substantive codes that reflect the substance of what people said or the observed events, actions, or other dimensions of the phenomena. Codes are then compared; similar codes are clustered and given an initial label and a category is formed. Further data collection and analysis will produce other categories. The last step in the grounded theory is exploration and elaboration of the links between the categories and the possible development of grounded theoretical patterns²⁵. In this research the methods of grounded theories will be used to support the data collection and analysis. However, the final part in grounded theory- that is, the development of theory- is not taken in this research.

One of the methods developed in grounded theory, and which was applied to the data collection of this research, was theoretical sampling. Theoretical sampling is the process of data collection for generating theory whereby the researcher concurrently collects, codes and analyses his/her data and decides what data to collect next and where to find them, in order to develop his/her theory as it emerges. Beyond the decisions concerning the initial collection of data, further collection cannot be planned in advance of the emerging

²³ Turner, A. B.

²⁴ Smith, K. & Biley, F.

²⁵ Turner, A. B.

theory. The emerging theory points to the next steps - the researcher does not know them until he/she is guided by emerging gaps in his/her theory and by research questions suggested by previous answers²⁶. In other words, sampling and analysis must occur in tandem, with analysis guiding the data collection²⁷. The criterion for judging when to stop sampling the different groups pertinent to a category is the category's theoretical saturation²⁸ that is when no new information is added to the category from the participants.

Grounded theory has been criticised for its treatment of previous theory. In grounded theory an attempt is made to condense previous theory, so in that sense it is taken as one of the data, but it is not used to build on or acknowledged as vital knowledge²⁹. In this research the previous theory- that is, the literature- was studied before the empirical work, to build on the previous knowledge rather than to treat it as just one of the sources as in grounded theory. Grounded theory has also been criticised for the danger that the research will be lost in coding and category schemes, which in some cases is unattached to the research³⁰. This danger is always present in analysing data where the knowledge on the phenomena that is being researched is limited. By studying the previous literature, and a pre-understanding of the phenomena by the author makes this danger less likely to influence this work. On the other hand the previous experience and pre-understanding can introduce the danger of prejudices on the phenomena. Gummesson pointed out that lack of pre-understanding could lead to serious shortcomings and be misleading. He also pointed out that lack of pre-understanding could affect the choice of the right research methods, the priority of relevant importance and the danger of believing people who are misleading for the research³¹. Although limited research has been done on the Icelandic fish industry the author claims that his previous knowledge and experience in the industry as a foreman and product manager for over

²⁶ Glaser, B. G. & Strauss, A. L.

²⁷ Strauss, A. & Corbin, J.

²⁸ Glaser, B.,G. & Strauss, A. L.

²⁹ Denzin, K. N.

³⁰ Denzin, K. N.

³¹ Gummesson, E.

10 years is an advantage rather than a disadvantage, and limits the danger of being lost in coding and category schemes.

II.2 Scope of the Research

Although the focus in this research is on the two marketing companies the scope of the research involves a greater number of companies, including producers, the population of which has varied over time, and also subsidiaries of marketing companies. To get a better picture of the research site and the business of the two marketing companies the scope of the research is drawn up in figure II.1.

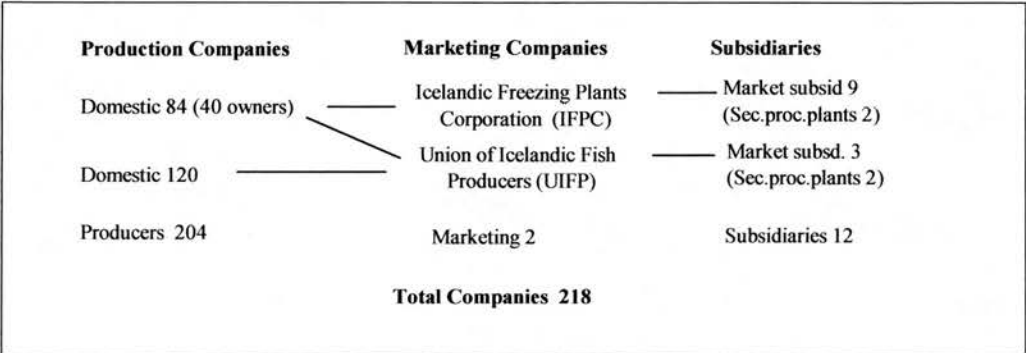


Figure II.1The scope of the research and number of companies

Some of the producers are both in the business of IFPC and UIFP and in many cases the managers of the production companies have an experience of business relationships with both companies. The number of companies has varied a lot over the last decade and even during this research but the number in the figure is a close estimate, as it looked half way through the research. These changes in the number of companies in the industry are mainly due to concentration in the industry where companies have merged. In addition to the companies, information can be drawn from people who are not working directly in the business but have either been in the business or have good knowledge of what has happened in the field. In its simplest form the scope of the research therefore consists of four main groups; the marketing companies, the subsidiaries of the marketing companies, the production companies and finally the people outside these companies. The last group, that is people outside these companies, consists for example of former employees, board members of the participants’ companies, consultants, mangers of competing companies and finally academics that

have knowledge of the development in the industry. In addition to these four groups are different levels inside the participants' companies. One way of analysing the different groups is to split the network into two levels:

- Strategic level, where the strategy, structure and overall governance is, or should be decided. This level includes the senior managers in the companies.
- Operational level, where the main day-to-day operation is managed. This level includes production managers and foremen on the processing site and sales persons on the marketing site.

Due to the small size of most of the production companies the boundaries between these levels are not necessarily clear; for example general managers of the production companies are in many cases also responsible for the marketing connection of the production companies and therefore in more contact with the market than the foreman or production manager. In this research the interviews are mainly aimed at the strategic level of activity.

Although the main emphasis in this research was placed on the senior managers in the participants' companies, interviews were also taken with other employees in those companies to get more depth in the analyses. Some of the interviews were more in the form of conversation where field notes were taken after the conversation took place. The total number of interviews was 33, with 31 people, as can be seen in table II.1.

	Nr. of interlocutors	Nr. of interviews
Managers and staff of the marketing companies	11	13
Managers and employees of the marketing subsidiaries	4	4
Managers and employees of production companies	9	9
Other as former managers of marketing, and production companies	8	8
Total	31	33

Table II.1 Numbers of interlocutors and interviews

In addition to the formal interviews are a number of conversations with managers and employees of the participants' companies and others that gave both vital information and clarified certain matters. Memos were also taken from some of the conversations and used as a source of data for the analysis of the two cases.

The key to the selections of the interlocutors was the importance of the interlocutors, accessibility and knowledge of the phenomena that were

studied in this research. The importance is based on the position of the interlocutors in the companies as well as how well they represent different views on the relationship between producers and the marketing companies. In selection of the interlocutors, the different approach of the companies to the relationship was also taken in account. The sample taken in this research was not selected beforehand but rather, according to the analysis of the interviews and documentation, as is the case in theoretical sampling³². The fact that interlocutors were not chosen by random sampling brings up the risk that the interlocutors may not represent the sample well enough. Due to the limitations of this study in terms of time, size and single research, it was considered more dangerous to take a random sample, which would be difficult to access and would not guarantee in any way different views that would be represented. Selecting interlocutors in accordance with their views, impact and knowledge was considered to serve the aim of this research much better.

II.3 Data collection and analysis

The empirical research was split into two main parts. Part one is a descriptive analysis of the history of the two companies, providing the background and context for the second part, which is the analytical component of the two case studies. In the second part the main emphasis is on the last 15 years when the Icelandic economy started to become more open and market oriented (see Chapter III). During this period the first sign of major changes in the operation of the marketing companies started to emerge. The main focus in this part is on the period from 1985 until 1998, during which the marketing companies have gone through major changes in their operation, making them much more international in their marketing orientations. Significantly, it was during this period that their ownership form changed from being co-operative to becoming limited liability companies.

Data collection in the first stage of the research was more focused on secondary sources materials/data such as the companies' annual report,

³² Strauss, A. & Corbin, J., 1990.

newspapers, articles, official reports, companies' newsletters and history of the companies. Although the main emphasis was on the historical secondary data, primary data was also gathered, especially where interpretation of the history is important for the research. Small scale interviews were also used to clarify some aspects of the history where it is believed to be important for the research and interviewers were available. The first part of the research, the historical development and writing up the case as well as the literature review build up a firm base of knowledge for the next step that is the interviews.

The emphasis in part two of this research was on the collection of data through interviews. Here, the research effort was based on in-depth semi structured interviews, whereby as Bryman claims "*the investigator uses a schedule but recognises that departures will occur if interesting themes emerge from what respondents say and in order to get their version of things.*"³³ Hence the emphasis was on having the respondents using their own words in answering the questions³⁴. The aim of these interviews was to get a more independent view of participants' perceptions on the topics of the three research questions (i.e. the structure and governance on the alliances as well as the role of the central firm). The interviews lasted from half an hour to three hours. One interview was conducted by phone and lasted half an hour but others were conducted face to face. One of the problems in conducting the interviews was that the interlocutors were very concentrated in using their own language or wording of the topics of the research. Most of the interlocutors were either former or present senior managers that had a very strong opinion/view of the development of the network. Due to this the interviews turned out to be more unstructured than initially planned. The weakness of these rather unstructured interviews was that they would not be as comparable as structured interviews³⁵. To avoid this weakness the topics for the interviews were clear and covered in the interview although the interlocutors were not asked exactly the same questions. The questions

³³ Bryman, A., page 149.

³⁴ Bryman, A.

³⁵ Bryman, A.

that were prepared for the interviews where therefore more or less used as a direction for the discussion and a checklist to guarantee that all the topics listed were covered. The historical analysis undertaken in part one of this research as well as the author's previous knowledge of the companies' operation turned out to be very helpful, allowing the author to pursue interesting matters that came up in the interview and to take actual examples to ask the interlocutors to explain. The mixture of unstructured interviews and pre-understanding was therefore an advantage and made the interview and data collection better focused and deeper than it otherwise would have been.

The interviews were conducted in three phases. The first phase commenced in the summer of 1997 when six interviews were taken with selected people from all levels in the study. The interlocutors were selected to give as broad picture of the research site as possible. These interviews were then coded and analysed. The analyses were then used to reconsider the topics for the next phase of the data collection, which took place in the summer, and autumn of 1998. In this phase eighteen formal interviews were taken. These interviews were coded and analysed in the winter 1998/99. The last phase in the interviews took place during early 1999 with 8 people. The aim then was to fill in gaps that had been identified in the analyses and to cover the spectrum of the sample group. As a example of this gap, it became clear that no interlocutors talked about marketing fish products but only about selling the products. This topic was taken further and asked about in the interviews, which lead to more emphasis being put on questions about the role of the central firm in the value creation in the network. During this time other data was collected as documentation that was used in the analyses of the two cases. This sequence of collecting data and analysing them is in accordance with the theoretical sampling described by Strauss and Corbin³⁶ earlier in this research methods chapter.

Most of the interviews were taped. If the interview was not taped notes were taken immediately after the interview. Not all interviews were transcribed in whole. According to Strauss and Corbin (1990) the rule of

³⁶ Strauss, A. & Corbin, J.

thumb is to transcribe only as much as is needed. In accordance to that the first interviews were transcribed in whole but after that, only the parts of the interviews that were important for the analysis were transcribed. The QSR Nud•ist Revision 4.0 software was used to code and group the transcripts of the interviews.

II.4 Ethical Considerations

When planning research it is important to realise from the beginning how the study might impact upon the participants and thus it is important to ensure safety, anonymity and confidentiality of the individual. Bryman claims, that in researching organisations the *“investigator must be sensitive to the ethical and political dimension of the study”*³⁷. In a similar way Bulmer, claims that ethical considerations for organisation studies need to take into account *“invasion of privacy, [whether] there is a lack of informed consent on the part of those studies, [whether] people are deceived and [whether] there is the possibility that harm could come to those studied”*³⁸. In accordance to this the participants have the right to get information, so an information, sheet was given to participants to ensure that they know about the nature and the purpose of the study, and the methods for collecting and analysing data. It was also highlighted at the beginning of each interview that the process of the research might change due to the fact that this was a mixture of quantitative and qualitative research and because the project develops and changes with ongoing data analysis. It was emphasised in the information sheet that participants had the right to terminate participation in the study and resist questioning at any time without any penalty. They were also asked to sign an informed consent declaration before the beginning of the study to show their explicit agreement of participation. Due to circumstances, three interlocutors neither received the information sheet nor signed the confidential statement. They were provided with verbal explanation of the research where they were promised full confidence as all other participants.

³⁷ Bryman, A., page 3.

³⁸ Bulmer, M., page 217.

The participants also had the right to anonymity, confidence and privacy. Their actual names were never used and nothing is reported which might be traced to a particular participant. Each interlocutor was given a coding, which is used when he or she is quoted in the thesis. Only the author has access to this coding. However, full confidentiality could not be promised because words and ideas are used in the final report. The participants were informed that selected excerpts would be used in this final report, with minor changes to details, if needed, so that they could not be recognised. Numbers rather than names were written on the tapes, and a matching list of names stored separately, in my office, to ensure anonymity. All data remain confidential and tapes will be destroyed when the study has been examined.

II.5 Limitation to the study

Limitations of the study refer to those issues which diminish the validity of the study. First of all, the number of cases (that is, only two) is small and limits the ability of generalising the findings of this study.

Bresnen M points out that the reactive, unstructured type of research approach is a double-edge sword or as he claims *“on the one hand, it yields valuable information and insight in a way in which a more pre-planned and structured approach does not; on the other hand, you lose the benefits of a more exactly comparable database that you would otherwise have obtained using the latter approach.”*³⁹ In a similar way Bryman claims that in multi-site studies the data needs to be comparable and it is therefore necessary to use more structured methods of data collection than for just one case⁴⁰. The research methods used in this research limited the generalisation ability, but it is however claimed that using the semi-structured interviews brings more rigour to the research than fully unstructured data collection.

During the research time both the networks were going through major changes in their operation that could have affected the openness of the interlocutors in the interviews. This can affect the research but in the same way it meant that some of the interlocutors were even more open to express

³⁹ Bresnen, M., page 47.

⁴⁰ Bryman, A.

their thoughts about the network and philosophised a lot about different possibilities of the development of the network, both in the past and in the future. On the other hand this also meant that some interlocutors were very careful about expressing their thoughts about the development, being afraid of their position and status inside the companies and network. This was especially true for IFPC, which was going through difficult times in 1998 and 1999 leading to changes of president of the companies and reductions of other staff. On the other hand UIFP was on the way up, diversifying its operation quite a lot and with many new managers inside, making the atmosphere in the companies different.

All the interviews were taken in Icelandic and coded in Icelandic. The quotations were then translated into English, which is not the first language of the author. Hence, the danger is that in the translation some of the nuances of the language will not be made as explicit in the English translation as in the original Icelandic.

Despite the justification of the research methods, as described earlier, it has to be recognised that generalising from two cases limits the use of the findings of this research. The research is analytical and explanatory with the aim of contributing to the identified gap in the literature about the strategic alliances and networks for SMEs companies. The research should be viewed in that light and no other.

II.6 Human Perceptions

One of the problems conducting research like this is human perception that is, how different people view and understand the phenomena being investigated. This became clear in this research where the interlocutors had a very strong need to tell the story about the development of the network in their own terms. As a researcher it was often difficult to judge whether they were explaining the situation as they saw it or as they wanted it to be. It has to be considered that in many cases the interlocutors were salesmen with lots of experience and talent in selling products by explaining the quality of the products. As a researcher I often felt like a prospective buyer who needed to be convinced about the product quality without seeing it. Hence,

it became clear that the interlocutors were explaining the situation as they wanted it to be rather than the real situation. As the interviews went on and it was possible to go deeper into the subject, the interlocutors started to describe the situation and the network more realistic. Understanding of the phenomena and the background information gathered from the historical analysis of the companies played a big role in breaking this “salesman” perception of the interview. In the same way the rather unstructured interviews that were conducted opened the possibility of taking the topics further, asking for real examples to highlight the reality rather than the “salesman’s” virtual reality. In most cases the interlocutors were very honest and open about the topics and willing to explain how they have seen the development and key issues of the network. In evaluating the effect of human perception on the research it has to be considered that both the networks were going through major changes during this time, which could easily have affected the interlocutors and their views of the development of the network. The conclusion is that the background information from analysis of the history of the companies, as well as previous knowledge of the companies and the fish industry, made the interviews much more effective than they otherwise would have been. Hence, it was possible to compare the interviews with the history during the interviews themselves, thereby making the interviews deeper than they would have been if the comparison had been done afterwards.

III Background

The aim of this chapter is to give a short overview of Iceland and the Icelandic economy and society, which form the background of this research. The main emphasis will be on factors that are important to understanding and getting a holistic picture of the environment and society which surrounds the Icelandic fish industry, and how it has developed over this century. The discussion starts with simple facts about Iceland, its geography, history, demography and culture. The next section discusses the basic facts and figures in the Icelandic economy and then the discussion moves on to what has characterised the economic policy in Iceland from the beginning of this century to the year 1997. In the conclusions the discussion is drawn together by looking at the competitiveness of Iceland as well as its strengths and weaknesses.

III.1 Geography and Climate

Iceland is an island in the north Atlantic and is a part of the European continent. The nearest neighbours are Greenland (287 km away), Faroe Island (429 km away), Scotland (798 km away) and Norway (970 km away). The size of Iceland is about 103,000 km² comprising waste land 50.5%, grazing 19.5%, glaciers 11.5%, lava 10.5%, sands 4%, lakes 3% and cultivated land 1%¹. Most of the coast of Iceland is characterised by fjords with good natural harbours except the south coast, which is mainly sand beaches with no fjords, and therefore no natural harbours. Despite the location of Iceland the climate is not as cold as the name suggests, due to the Gulf Stream that comes to Iceland along the south west coast where it reduces the influence of its location so close to the Arctic Circle. In a normal winter the Icelandic coast is ice free although occasionally drift ice may sweep up to the coast. In the history of Iceland there have been winters when the west and north coast were covered with ice for some time, blocking all ways to the sea. This happened last in 1918 in an extremely

¹ Landshagir 1998.

cold winter. In a normal year the average temperature in Reykjavík in January is around -0.5°C but in July around 10.6°C .

III.2 Natural resources

Iceland is not rich with natural resources; the most obvious one, and that which has the most economic importance, are the fishing grounds that surround Iceland. Other natural resources are the energy resources in the form of hydroelectric- and geothermal power. In 1993, 4,950 Gwh of electricity was exploited of the 45,000 Gwh that are estimated to be economically exploitable in Iceland, or around 11% of exploitable energy. In 1993 geothermal power was used to heat 86% of apartments in Iceland. Almost 100% of electricity consumed in Iceland comes from water- and geothermal power. Large scale industry such as Aluminium smelter and Ferro-silicon smelter consumed 47% of the electricity in 1993, and plans for expansion of that kind of high power consumption industry are now on the way. The third important natural resource is the natural beauty of Iceland, which attracts increased numbers of tourists to Iceland each year. In many ways there are contrasts between the increased emphasis on building of hydroelectric power stations and the tourist industry, which uses the unspoiled nature of Iceland as an attraction. The building of hydroelectric power station demands that a lot of land goes under lakes, power lines have to be laid over unspoiled areas and waterfalls could be affected from changes of the flow of rivers, all of which could affect areas that at present have great tourist attraction.

III.3 History

Norwegian Vikings who were escaping from the domination and taxation of the Norwegian monarchy found Iceland in 874. The settlement of Iceland came mainly from Norway, although a considerable proportion came from the British Isles, especially Ireland and the Hebrides². In 930 the Icelandic parliament "Althing" was established at Þingvellir. In 1262 Iceland became part of the Norwegian monarchy and in 1380, when Norway became part of

² Kristjánsson, L., volume 4.

the Danish monarchy, Iceland did as well. In 1874 the Danish monarchy granted Iceland a constitution, which was followed up by granting Iceland a home rule in 1904 and the first Icelandic government minister. Iceland got full control of virtually all its domestic affairs in 1918 although still with the Danish King as head of state. Full establishment of the Modern Republic of Iceland was in 1944 when Iceland became an independent parliamentary democracy with a President as head of state. Icelanders have maintained their language with little change from the settlement of Iceland, despite having been a part of other nations most of the time since the land was found. Until this century the Icelandic nation was a farming society, that is, people lived on the land, and it is only from the latter part of the 19th century that villages began to develop. Although Iceland was a farming society it would not have survived without the support from the sea and fish has always been an important part of the Icelandic diet³.

III.4 Demography and culture

At the end of 1996 there were 269,735 inhabitants in Iceland, which is a 0.72% increase from 1995. In 1801 the population of Iceland was around 50,000 and in 1901 the population was around 80,000, so the increase has been very fast in this century. Iceland is one of the least densely populated countries in Europe with around 2.6 inhabitants per square kilometre. Approximately 86% of the population live in communities with population in excess of 1000 inhabitants⁴. Of the total population about 60% live in the area of the capital city Reykjavík. The largest town outside the capital area is Akureyri in the north of the country with 14,920. In the West Fjord (Vestfjörðum) Ísafjörður is biggest with 3,337 and in the east Egilstaðir is biggest with 1,580.

The standard of living in Iceland is high and very similar to that in the nearby countries, especially in the Scandinavian countries Norway, Denmark and Sweden. These Scandinavian countries and their social system have been the role model for Icelandic society. This is well reflected

³ Kristjánsson, L., volume I.

⁴ The economy of Iceland, Spring 1997 (Central Bank of Iceland).

in the high standards of systems such as education and health, as well as in other aspects of social services that are provided in the country. The vast majority (91.5%) of the population in Iceland are members in the Church of Iceland (state church), which is a Lutherans religion; the remainder are spread over different, mainly Christian religions.

III.5 Icelandic Economy

At first glance, the small size of the economy and how dependent it is on one industry, that is the fish industry and export of its product, characterises the Icelandic economy. In an other way the economy has a similar structure as most of others OECD⁵ countries, but for most of the post-war period the Icelandic economy has been characterised by extensive government interference, direct or indirect⁶. Since the mid-eighties the Icelandic economy has gone through an important transition to increase liberalisation and freedom, with, for example the establishment in financial- and stock markets in the way that is common in most western countries, and the deregulation of the economy. The government still has much influence on the economy and owns for example two of the four commercial banks in Iceland, and most of the investment funds are government controlled. However the investment funds have merged and been changed into Limited Liability Company, and the government sold its share in the autumn of 1999. The government also changed the ownership form of the commercial banks into limited liability, by 1st January 1998⁷, although it still owns the majority share in both the banks. The transition that started in the mid-eighties means that companies in Iceland are now operating more or less in the same financial environment as most companies in the western world.

III.5.1 Gross Domestic Product

In 1996, the gross domestic production (GDP) was approximately \$7.3 thousand million, which is small in absolute terms (somewhere around

⁵ OECD stands for "Organisation for Economic CO-operatin and Development"

⁶ Árnason, R.

⁷ The Economy of Iceland, Spring 1997.

0.67% of the UK economy), but in terms of per capita the GDP is approximately \$26,900, which is rather high by international standards⁸

Contribution of industrial sectors towards GDP 1973 – 1996				
	1973	1980	1990	1996
	%	%	%	%
<i>Fishery</i>	7.6	8.5	10.1	10.1
<i>Fish processing</i>	8.5	8.3	5.2	5.1
Fish Industry	16.1	16.8	15.3	15.2
Agriculture	5.5	5.2	2.9	2.2
Manufacturing	13.1	12.8	12.3	11.6
Construction	12.3	9.2	8.2	7.2
Trade, Restaurants, Hotels	10.5	10.9	11.5	13.2
Transportation	9.8	8.0	7.8	8.6
Public service	12.3	15.4	16.1	16.9
Other service	20.4	21.7	25.9	25.1
Total	100.0	100.0	100.0	100.0

Table III.1 Contribution of industrial sectors towards GDP⁹

The main trend over the last decade in contribution of various economic sectors to GDP is that agriculture has gone down from 5.5% in 1973 to 2.2% in 1996. The largest increase has been in the service sector, as can be seen in Table III-1, where the biggest increase is in areas like trade and financial service. The fish industry counts only directly for around 15% of the total GDP although it stands for around 72% of the commodities exported from Iceland¹⁰. The private and public service sectors are in relative size and structure very similar to other OECD countries¹¹. On the other hand the manufacturing sector is very small and simple where the main emphasis lies on few big high power consumption companies like Aluminium and Ferro silicon smelter.

III.5.2 The Labour Market

The labour market in Iceland in 1995 was approximately 130,254 people. The participation rate in the labour market has dramatically increased over the past decades mainly due to increased participation of females in the labour market. In 1983 the labour market was estimated to be 78% of the

⁸ The Economy of Iceland, Spring 1997.

⁹ Magnússon, S. M.. Figures from before 1973 are not available in this form.

¹⁰ The Economy of Iceland, Spring 1997.

¹¹ Árnason, R.

population among 15 and 74 years of age¹². The corresponding figure for the year 1997 is approximated to be 81% of those aged between 16 - 74 years old¹³.

Most Icelandic employees between 90-95% of the total work force are members of trade unions, which is higher than in other western countries where the figures are, for example, Denmark 86% Sweden 87.7%, UK 43.3%, and France with only 12.0%.¹⁴. Most of the trade unions in the private sector are affiliated with the Federation of Labour, which in most cases takes care of negotiation with the Federation of employers. In the public sector individual trade unions are affiliated either with the Federation of Public Employees or Federation of University Graduates, which then take care of wage negotiation with the state. Most of the companies in the private sector are members of the Employers Federation or Federation of Cooperative Employers, which take care of wage negotiations on their behalf. This arrangement, that is a high percentage of employers and employees connected to a larger Federation, has brought with it large wage negotiations and guidelines are set for other smaller unions. As part of this negotiation the government usually announces its part in the negotiation in the form of changes in taxes and benefits in the social welfare system. In the past, there has been increased pressure to break down this large wage negotiation and instead put more emphasis on negotiations within a rather wider framework between the big federation of the trade unions and between the employers and the individual company. The labour union within companies then would negotiate the detailed matters concerning the company and its employees. Increased freedom and changes in the business environment as well as increased difference between companies will probably create more pressure for wage negotiations in a form like this. This will probably mean the establishment of trade unions in individual companies, which is not common today.

¹² Árnason, R.

¹³ Landshagir 1998.

¹⁴ Snævarr, S.

From 1989 onwards, the labour market has been relatively stable and few strikes disturbed it until 1997 when increased pressure from the employees for their share in the improved economy caused a few strikes, but very few spanned a long time period. Before 1989 the labour market was rather unstable and strikes very common mainly due to an unstable economy and high inflation. An example of this unstable labour market occurred during the time period 1977-88. The working days lost in strikes was close to 0.2%, which is a much higher percentage than is known in most of the Nordic countries¹⁵.

Employment by industries reflects very well the changes that have occurred in Icelandic society in this century. The most obvious changes are the decline of employment in agriculture where in 1940 it counted for 16.4% of the total work force but in 1995 the rate was down to 4.9%¹⁶ (see table III.2).

Development in Employment by industries 1970 - 1995				
	1970	1980	1988	1995
	%	%	%	%
<i>Fishery</i>	6.6	5.3	5.2	5.2
<i>Fish processing</i>	7.8	9.1	6.7	5.9
Fish Industry	14.4	14.4	11.9	11.1
Agriculture	12.4	7.9	4.9	4.5
Manufacturing	15.2	15.2	13.3	11.3
Construction	10.7	10.2	9.3	7.9
Power stations	0.7	0.9	0.9	1.1
Trade, Restaurants, Hotels	13.5	13.4	16.0	14.8
Finance, Real Estate, Insurance	10.9	12.6	15.3	16.4
Transportation	8.4	7.3	6.6	6.8
Government	12.4	15.7	17.4	19.8
Other	1.4	2.4	5.4	6.3
Total	100	100	100	100

Table III.2 Employment by industries¹⁷

In Employment the fishing industry has also declined over the past decades, from 15.3% of the total work force in 1965 to 11.1% in 1995. The largest increase, on the other hand, has been in the service sector. Compared to the

¹⁵ Árnason, R.

¹⁶ Magnússon, S. M.

¹⁷ Sögulegt yfirlit hagtalna 1997.

Nordic countries the picture of employment is very similar but with more employment in the primary processing sectors like agriculture and fishery¹⁸.

The labour market is characterised by a generally long working week, with average weekly hours of the total work force around 46 hours. The normal working week is 40 hours so this means general overtime work which can be traced to a rather low hourly wage¹⁹.

III.5.3 Foreign Trade

Foreign trade plays an important role in the Icelandic economy and in 1996 export of goods and non-factor service accounted for around 36% of the total GDP. Around 70% of foreign trade consists of commodities, the remainder are services²⁰.

Products / Years	1960-67	1968-73	1973-79	1979-87	1988-92	1993-96
	%	%	%	%	%	%
Fish	91.3	79.7	74.3	74.0	75.4	74.6
Agriculture	5.1	4.6	2.7	1.6	1.8	1.8
Manufactured	1.6	15.2	21.3	22.7	20.4	19.5
Miscellaneous	2.0	1.5	1.7	1.7	2.4	4.1
Share of commodities in total export	64.6	61.7	70.0	71.1	72.8	N/A

Table III.3 Composition of commodity exports²¹

As can be seen from Table III.3 fish products stand for around 74.6% of total export of commodities in the years between 1993-96 but around 91.3% in the years 1960-67; the percentage of the export before that time was around 90%. The changes in export are mainly that in the years 1968-73 manufacturing products became much stronger, from 1.6% of the commodity export to around 15%, and have been around 20% since then. This is mainly due to the export of aluminium and ferro-silicon; export of these stood at around 63.4% of the export of manufacturing products between the years 1993-96.

Iceland's main export markets are the EEA (European Economic Area) countries. In 1996 the UK was the most important with 19.2% and then

¹⁸ Snævarr, S.; Árnason, R.

¹⁹ Árnason, R.

²⁰ Árnason, R.

²¹ Árnason, R.; The Economy of Iceland, Spring 1997.

Germany with 13.0%. After these two EEA countries US came next with 12.6% and then Japan with 10.4% of the total commodity export (see Figure III.1).

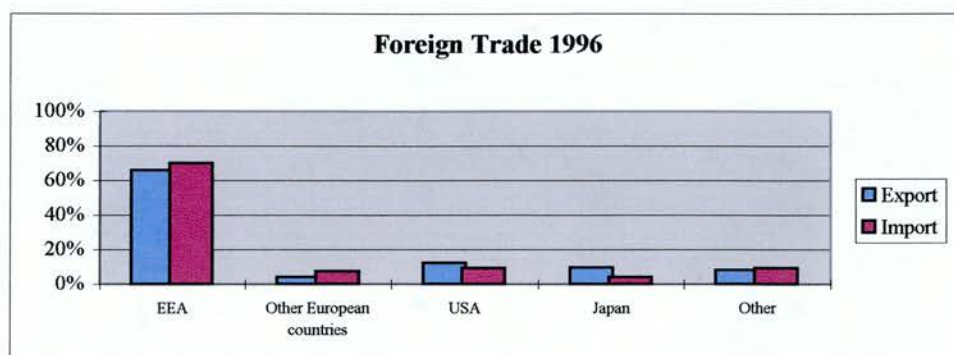


Figure III.1 Geographic Distribution of Foreign Trade in 1996²²

In the same way as in export around 70% of all imports come from EEA countries where the UK is again the most important with 10.2% of the total value of imported goods. USA is the next largest with 9.4% of the total value of import but Japan has only 4.0% of the import against 10.4% of the total value of export (see figure III.1).

In Table III.4 is the breakdown of imports of goods into groups for the years 1970-96. The biggest group is raw material and fuel, which accounts for around 35.7% of the total import in the years 1993-96 and of that, raw material (industrial supplies) counts for 27.8% of the total import.

	1970-74	1975-79	1980-84	1985-88	1989-92	1993-96
	%	%	%	%	%	%
Consumption goods	33.5	32.3	34.6	37.2	28.6	31.3
Raw materials and fuel	30.3	35.9	35.9	30.7	35.5	35.7
Investment goods	36.2	31.8	29.5	32.1	35.9	33.0

Table III.4 Composition of commodity imports²³

Participating in international organisations is very important for small nation like Iceland, both to get access to markets as well as to minimise the danger of becoming isolated and uncompetitive in the international market. Table III.5 gives an overview the participation of Iceland in international organisations.

²² The Economy of Iceland, Spring 1997,

²³ Árnason R.; The Economy of Iceland, Spring 1997.

Iceland's Membership in International Organisations	
International Monetary fund (IMF)	1945
International Bank for Reconstruction and Development (World Bank)	1945
United Nations (UN)	1946
North Atlantic Treaty Organization (NATO)	1949
Organization for Economic Cooperation (OECD)	1949
Council of Europe	1950
Nordic Council	1952
International Finance Corporation (IFC)	1956
International Development Association (IDA)	1961
General Agreement on Tariffs and Trade (GATT)	1964
European Free Trade Association (EFTA)	1970
Conference on Security and Cooperation in Europe (CSCE)	1975
Western European Union (WEU)	1992
European Economic Area (EEA)	1994
World Trade Organization (WTO)	1995

Table III.5 The year Iceland joined international organisations²⁴

III.5.4 Investment and Interest Rate

Investment in Iceland has for the last decades been around 25% of GDP, which is a little higher than OECD or EU countries (see Table III.6). The investment reached its peak in 1974 when it was 32.1% of the total GDP mainly due to huge investment in stern-trawlers, electric power generation and distribution systems for power²⁵. Government plays big a part in the investment in Iceland, or around 30% of the total investment, mainly due to the fact that the government owns most of the power plants and their distribution and communication systems. Industry invests around 45% of the total investment in Iceland, and residential construction is around 22.0% of the investment (see Table III.6)

²⁴ The Economy of Iceland, Spring 1997.

²⁵ Bjarnason, A.

Investment by sectors and industries 1960 - 92					
	1960-67	1968-73	1973-79	1979-87	1987-92
	%	%	%	%	%
Industry	49.3	44.4	41.6	45.6	44.6
Agricultural	9.4	6.7	5.8	5.3	3.5
Fishery	13.0	10.1	12.0	10.1	9.2
Manufacturing	7.4	13.0	8.9	10.4	9.2
Transport	10.8	7.1	6.4	6.0	9.0
Other	8.7	7.6	8.5	13.5	13.7
Residential Construction	23.1	21.2	22.9	22.6	22.8
Government	27.5	34.4	35.5	31.8	32.7
Energy	7.7	13.6	17.8	12.5	8.6
Communication	12.4	12.8	11.0	12.1	12.3
Buildings	7.4	8.0	6.7	7.2	11.8

Table III.6 Investment by sectors and industries²⁶

Over the last decade a large part of the investment in Iceland has not been paid for or supported by voluntary savings (less than 40% in 1990). Pension funds, official investment funds and foreign borrowing have paid for the rest. This little voluntary saving in Iceland over this time can be explained by high inflation and negative real interest rates but the interest rate was negative from 1960 to 1990 (see Table III.7).

Comparison of average real interest rate 1960 - 1990						
	1960-67	1968-73	1974-79	1980-87	1987-90	1960-90
	%	%	%	%	%	%
Iceland	-1.8	-7.3	-14.5	-1.8	8.1	-4.1
UK	2.7	2.0	-2.0	3.5	3.4	1.9
USA	2.2	0.6	-0.6	5.4	5.0	2.5

Table III.7 Average real interest rate²⁷

The stock market, more options on the financial market and high real interest rates have supported voluntary saving and opened more interesting options for saving than was known before 1990. Hence, because voluntary saving is lower in Iceland than most other western countries it has been one of the main aims of past governments to improve this situation.

²⁶ Árnason, R.; Sögulegt Yfirlit Hagtalna 1993.

²⁷ Árnason, R., page 23.

III.5.5 Inflation

From the end of the Second World War (WW2) until 1990 Iceland has suffered from economic fluctuation and high inflation²⁸. During the years 1980-90 the average annual inflation in Iceland was 34.9% compared to an average 6.9% in EU countries. Inflation reached its peak in 1983 when it went over 80% on a one-year basis²⁹. After 1990 the government has managed to get the inflation down to a level which is known in other western countries and it has since been even lower than in other neighbour's countries. The inflation rates between the years 1956-96 are illustrated in Figure III.2 where it can be seen that Iceland has for a long time until 1990 suffered from much higher inflation than in other OECD countries or in important market countries such as the UK.

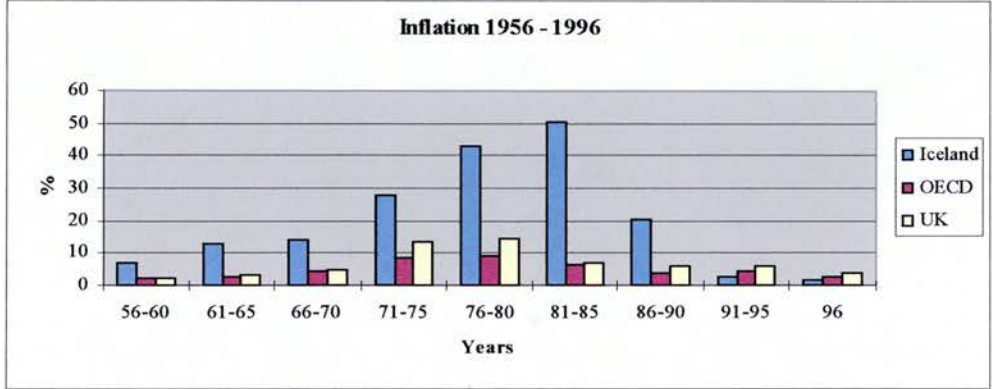


Figure III.2 Comparison of inflation 1956 – 1996 (rates averaged over 5 years)³⁰.



Figure III.3 Inflation in Iceland 1955 – 1996 (year-on-year rate)³¹

²⁸ Árnason, R.

²⁹ The Economy of Iceland, Spring 1997.

³⁰ Snævarr, S.; Sögulegt Yfirlit Hagtalna 1995.

In figure III.3, which illustrates the inflation in Iceland on a yearly basis between the years 1955-96, it can be seen that inflation has been fluctuating over the last decades. Most of the time inflation has been very high and it is not until recent years that the government has gained control over it.

III.5.6 Economic Policy in Iceland

Economic policy in Iceland has changed over time; these changes can be divided into periods with different aims and methods for managing the economy. The economist Magnús S. Magnússon split the development over the last century into three periods³²:

- 1) 1876-1930, a period of minor government interference
- 2) 1930-1960, a period of regulated economy and major credit transfer between economics sectors
- 3) 1960-1990, a period of slow adjustment to a market economy.

In addition, it is logical to talk about the period from 1990 until now as a period of market economy although with some exceptions, for example the ownership by the government of the commercial banks and investment funds. In the following discussion these four periods will be used as a guideline to describe the Icelandic economy, its policy, aims and main characteristics over the last century³³.

III.5.6.1 Minor Government Interference 1876-1930

This period is highly influenced by the farming society that existed in Iceland during this time, although mainly before the First World War (WW1). The value of the society is reflected in economic policy by factors such as not depending too much on loans but rather saving before buying. Formally Iceland did not get independent registration of its own currency the “króna” until 1922; until 1914 the Icelandic “króna” had the same value as the Danish “króna”. In 1924 the Icelandic government broke the tradition

³¹ Landshagir 1998. The inflation is measured as a change in the consumer index with January-March 1939=100

³² Magnússon, S. M.

³³ In this discussion the author will support Magnússon's discussion about the economic policy during that time

of letting the bank system control the value of the currency and started to interfere directly with how the value of the Icelandic “króna” was registered. From this time onward, the currency was valued according to the need of industry, mainly the fish and farming industries. The main aim of the economic policy during the last decade of this period was to have a balance between import and export, which was done with having fixed registration of the “króna” for the longest run in the history, from the years 1925-35. During the period 1901-30 the economic growth was on average 3.9% per year though with very little growth over the WW1 period but rapid growth (6.2%) between 1920-30. During the period 1900-45 the economic growth was rather high in Iceland (3.5% average increase in GDP per year) compared to 2.5% in the US, 2.2% in the UK and 2.0% in Denmark³⁴. This can be traced to the fact that Iceland was at this time transferring from a farming and fishing society to an industrial society, like those which were already well established in other western countries³⁵. The main characteristic of the economic system during the period between 1900-30 was freedom and little government interference³⁶.

III.5.6.2 Government Interference 1930-1960

The time until 1960 was characterised by increased regulation and barriers that the government implemented in the economy. The barriers were for example high import taxes on goods that were described by the government as being “unnecessary”. As a indication of the way of thinking during the period of 1934 – 38, the aim of the government was to implement “planned economy³⁷”, not just out of necessity but rather because it was believed to be a vital part of the scientific management of economy³⁸. The aim for “planned economy” did not work out and the economic policy was clearly a move away from freedom and markets, towards an economy which was

³⁴ Snævarr, S.

³⁵ Snævarr, S.

³⁶ Magnússon, S. M.

³⁷ “Planned economy” is economy similar to what was practiced in the Eastern Europe in the time of communist government there with main emphasis on long term planning.

³⁸ Snævarr, S.

managed with direct interference of the politics with regulation, barriers and government intervention³⁹. The economic growth was slow during the period 1930-37 (on average 1,4% per year), and export was difficult due to general economic depression on foreign markets. This also affected unemployment, which rose during this time mainly because of difficulties in selling salted Cod to the Mediterranean countries.

Due to the military occupation of Iceland, first by the British army and then later the US army, Iceland benefited greatly during the WW2 period unlike most other countries. This military occupation brought with it increased domestic activities like building roads and airports using the Icelandic work force. Many talk about the period of the WW2 as a transformation period for Iceland, going from a rather poor and simple conservative farming and fishing society to become one of the richest nations in the world with living standards which were unknown to most Icelandic people before that time. During WW2 Iceland gained an increase in the GDP of around 38%, or on average 5.5% increase in GDP per year and in its peak in 1940 a 9.5% increase⁴⁰. This boost to the Icelandic economy cannot all be traced to the increase in domestic investment and activities due to the military occupation. During WW2, the UK government made an agreement with Iceland about importing fish from Iceland amongst other things to help with the food supply for the UK, which was very difficult during this time. This arrangement, and war activities in the world, meant that Icelandic fish dominated the UK market for fresh iced fish and this domination was reflected in high prices, which helped the Icelandic fish industry at a time when other traditional markets were closed⁴¹. The years from 1938-45 were therefore characterised by great expansion in the economy with decreased unemployment. The period after WW2 started with three years of depression and over-controlled economy. In the years 1950-55 there was

³⁹ Snævarr, S.

⁴⁰ Snævarr, S.

⁴¹ Snævarr, S.

rapid economic growth but after that, until 1960, the economy was rather unstable with little economic growth⁴².

From 1939 the Icelandic government had to face managing the economy, which was highly index-linked, which meant that devaluation of the currency directly affected salaries and prices. Hence, controlling cost in the main industries like fishing and agriculture was increasingly difficult, so the government decided to use major transfer of credit between economic sectors to try to even out the fluctuation that followed the increased cost. In summary, one might say that the economy period from 1930-60 was characterised by separate or holistic measures which could include establishment of fund systems, transfer of credit, rationing processes and barriers in forms of legislation and regulation, which all adds up to an economy that was managed by political “hand power”⁴³.

III.5.6.3 Adjustment to International Business Environment 1960-1990

In the 1960s the Icelandic government started to adjust the rather closed economy towards a more open economy that took account of what was happening in other western countries during this time. The first step in this process was to obliterate the massive credit transfer systems and barriers. This development to open the economy went much slower in Iceland than in most other western countries and in many ways that real movement did not emerge until Iceland joined the EFTA⁴⁴ in 1970. Then external pressures and international contracts made it necessary for the Icelandic government to lower or remove some of the external barriers like very high import taxes on goods to Iceland⁴⁵. External barriers gradually declined as these international trade contracts were introduced but right up until the present day technical barriers are still protecting import of things like agricultural goods.

⁴² Magnússon, S.M.

⁴³ Magnússon, S.M.

⁴⁴ EFTA stands for “European Free Trade Association”

⁴⁵ Magnússon, S.M.

One of the main aims of governments in Iceland during this time period was to keep everyone in full employment⁴⁶. The government succeeded in doing this and from WW2 onward, unemployment was almost unknown, apart from between 1967-71 when the economy suffered from a drop in catch of important species like herring⁴⁷. Between 1971-90 the average unemployment rate in Iceland was 1,1% of the total labour force, compared to around 6% on average in the OECD countries⁴⁸.

One of the ways that the government used to defend the economy and keep unemployment down was to devalue the currency “króna”, and this happened rapidly over this period. In 1984 the government changed its policy in listing the currency when it implemented a fixed value for the currency, which worked for a limited time mainly due to an increase in fish catching and favourable conditions on major markets for fish⁴⁹. But when the catch declined due to over-fishing and unfavourable market conditions, the currency was devalued again. The policy of most governments during this time was to list the value of the “króna” in accordance with the needs of fish industry, which in many cases kept other industries in a poor competitive state⁵⁰. This was, in many ways, a barrier against more diversity in the economy, development of new industries and the strengthening of existing ones.

Other important characteristic of the economic policy during this time was increased and high inflation (see Table III.8 and Chapter III.5.5).

	1960-67	1968-73	1974-79	1980-90	1960-90
	(%)	(%)	(%)	(%)	(%)
Iceland	11.4	19.9	38.7	34.9	26.2
OECD	3.2	6.1	8.6	6.0	5.8

Table III.8 Average annual inflation: GDP implicit price index⁵¹

⁴⁶ Magnússon, S. M.

⁴⁷ Árnason, R.

⁴⁸ Bjarnason, A.

⁴⁹ Magnússon, S. M.

⁵⁰ Magnússon, S. M.

⁵¹ Árnason, R., page 31.

Every government had its aims set on getting inflation down but the met little success. However, there is doubt as to how serious this attempt was when the top priority was to minimise unemployment. Inflation between 1960 and 1987 was almost five times higher than in other OECD countries⁵² and reached its climax in 1983 when the year-on-year figure went over 80%⁵³.

It would be impossible to leave this period in Icelandic economy without mentioning the interest rate. With high inflation present in Iceland during this time, the real interest rate was negative most of this time and hugely negative (-14.5%) during the period of 1974-79⁵⁴. The government and the Central Bank of Iceland decided the interest rate until 1st of November 1983 when the commercial bank was given the freedom to decide⁵⁵. While the government controlled the interest rate, the real interest rate had no priority in the management of the economy, which was characterised by high inflation; high inflation meant a lower real interest rate⁵⁶. For businesses this meant subsidised loans, which worked almost like grants⁵⁷ and during this period it was the general view that getting a loan was like a bonus since inflation would eat up the loan.

The period of 1961-66 was characterised by rapid economic growth or around 8.8% increase in GDP per year, mainly due to a increase in the catching of herring. From 1967-69 on the other hand, there was a contraction of 3.5% of GDP due to the collapse of the herring stock in Icelandic water. During 1969-82, the economic growth was around 5.8% increase in GDP, mainly due to an increased catch as a result of expansions of the economic zone around Iceland of 50 miles in 1972 and then 200 miles in 1975⁵⁸. Other motives for economic growth during this time were the building of high power consuming industries, like aluminium smelter and

⁵² Árnason, R.

⁵³ Sögulegt yfirlit hagtalna 1993 - 1995.

⁵⁴ Árnason, R.

⁵⁵ Snævarr, S.

⁵⁶ Snævarr, S.

⁵⁷ Snævarr, S.

⁵⁸ Magnússon, S. M.

ferro-silicon smelter. These companies were built more or less with foreign money and owned by foreigners, particularly the aluminium companies but in the ferro-silicon company the Icelandic government had some share. As a consequence of this and a decline in fishing, the fish product in 1960-67 stood for 91.3% of the total export and manufacturing product 1.6% but between 1968-73 fish product stood for 79.7% and manufacturing products 15.2%⁵⁹.

Between 1980-90 the economic growth in Iceland was far less than the average in other OECD countries⁶⁰. There was a short period between 1986-87 with rapid economic growth, which caused very optimistic views, and huge investment, which the government pushed for with favourable loans from government investment funds. These investments were mainly in fish farming and fur bearing farming which turned out to be a bad mistake due to bad timing and unfavourable market conditions. The years between 1988-91 were characterised by great contraction and stagnation where inflation was declining but unemployment increasing.

The period from 1960-90 was characterised by unnatural economic conditions in the light of subsidised loans where the real interest was negative. The stock market was rather immature and companies had to get money in the form of loans rather than in the form of shares⁶¹. It can easily be said that economic conditions were never normal where the governments interfered with the economy in factors like devaluation of the currency, interest rate and control of loans, and where they never made profit a priority goal for companies, but rather the maintenance of employment levels. Although the governments slowly moved towards an open economy, their interference made businesses and the public suffer, because long term thinking was very difficult, leading to short term thinking and unrealistic activities and building. This environment also created political pressure to fix the bad condition. There was some ad-hoc political decision-making

⁵⁹ Árnason, R.

⁶⁰ Magnússon, S. M.

⁶¹ Magnússon, S. M.

like devaluation and increasing loans, rather than building up a healthy environmental framework from which managers and people could work.

III.5.6.4 Open Economy 1990-1999

In many ways 1990 was a turning point in the Icelandic economy mainly due to a wage contract, which was made in that year. A very broad settlement was made between all major players in the labour market, government, farmers and the banks, to lower inflation and to balance the economy, which had been rather unstable⁶². This settlement was named the “nation settlement” and held until the last wage contract took place in 1997, when trade unions pressed for higher salaries. The first evaluation of the wage contract, which took place in 1997, seemed not to threaten the goals of the “nation settlement” which were low inflation and stability.

The economy was in stagnation and downturn until 1991 mainly due to the restriction of fish catches and deterioration in terms of trade. In 1993 the GDP contracted by 3.3% but in the period 1993-95 the economic growth was more or less the same as in other OECD countries on average. In 1996 the economic growth was 5.7% which is well above the average OECD (which was little more than 2.0%)⁶³.

Inflation had been dramatically lowered and in 1993 and 1994 it was 1.5%, the lowest rate since the 1950s. Between 1994 and 1996 the year-to-year inflation was around 1.7%⁶⁴. Unemployment had also declined in the year 1996 to around 4.3%, from the year 1995 when it reached its peak of around 5.0% of the total work force⁶⁵.

The economic conditions have been rather favourable since 1993. There are many reasons for this but without a doubt one of the most important is the successful stabilisation the Icelandic economy, making it more stable than it has been for decades. The economy has moved from government

⁶² Snævarr, S.

⁶³ The Economy of Iceland, Spring 1997.

⁶⁴ The Economy of Iceland, Spring 1997.

⁶⁴ The Economy of Iceland, Spring 1997.

⁶⁵ The Economy of Iceland, Spring 1997.

interference to a much more open and market-driven economy with a financial and stock market as in most western countries. Recent governments have also emphasised privatisation of the economy and sold several state enterprises to the private sector⁶⁶. Included in this are companies like an insurance company (Íslensk endurtrygging), a fish processing company (Þormóður Rammi), a fish meal company (S.R.mjöl), a coastal shipping line (Ríkisskip), a tourist bureau (Ferðaskrifstofa ríkisins) and a heavy equipment plant (Landssmiðjan).

In addition to a more stable economy there have been many important structural changes implemented in the financial sector since the last decade. Among these are “interest rate liberalisation, elimination of automatic access to the Central Bank facility by commercial banks, liberation of foreign exchange regulations and establishment of foreign exchange market, establishment of securities exchange and leasing operations, and the development of secondary markets for public and private bonds.”⁶⁷ The Icelandic government has also adapted the Icelandic financial system to foreign financial markets within the framework of a Nordic Economic Programme 1989-92 and the implementation of the EEA agreement in January 1994.

Although the economy is gradually becoming more open and market driven and the direct interference of politicians is getting weaker, there is still a tendency to build up barriers around the economy. These barriers are for example to protect Icelandic agriculture with technical barriers against importing of foreign agricultural goods. Another barrier is against foreign investment in the Icelandic fish industry; foreigners are not allowed to invest in the fishery or fish processing sectors in Iceland. However, at the same time, Icelandic companies in the fish sector have invested in foreign companies in countries like Germany, UK, Chile, Mexico and Namibia.

The business environment is much healthier today than it was 10-15 years ago, and managers and owners of companies have to realise that they can not any longer count on the politician to come up with special measures to

⁶⁶ The Economy of Iceland, Spring 1997.

⁶⁷ The Economy of Iceland, Spring 1997.

change unfavourable conditions. The politicians, however, still have a tendency to interfere and put money into special situations like when they assisted fish industry in the West Fjord in 1994-95, by offering them favourable loans if specific conditions about improvements concerning effectiveness and profitability were fulfilled.

These changes of the economy towards an open and market-driven economy have taken a long time and are far from finished. It will probably take managers, politicians and private people some time to adjust their activities to the business environment which seems to follow today's economy.

III.6 Government and Political Environment

Icelandic government is built on a parliament system, which consists of 63 members elected from eight constituencies on the basis of proportional representation for a term of four years. Traditionally, between four and six political parties have members in the parliament "Alþingi". After the election in 1995, six parties had members in the parliament, where the two biggest parties, the Independent Party (right wing party) with 37.21% of the vote and the Progressive Party (central farmers party) with 23.3% of the vote, formed a coalition government. The four remaining parties are all left wing parties: the social Democratic Party with 11.4% of the vote, the Peoples Alliance with 14.3%, the Peoples' Movement with 7.2% and the Women's Alliance with 4.9% of the vote. Other parties that got a vote did not get members elected to the parliament. The number of members of parliament from each constituency is not proportional to the population, which means, that the constituency with the highest population is underrepresented and the constituency with the lowest population is over-presented. For example, the constituency with fewest inhabitants; the Western Fjord with 9,545 people have only 1,920 votes behind each Member of Parliament, compared to the capital area with 156,513 inhabitants and 5,448 votes behind each member of the parliament. Traditionally the governments have been formed by a majority coalition of two or more political parties. The government must be supported by a majority of the members of the Parliament to remain a power. The Prime

Minister and other Ministers exercise power and constitute the government. President is the head of the state but with very little political power although (s)he has to sign all new laws and has the authority to send them back to the parliament, but historically the president has never exercised that power. The other main power or political role that the president has is nominating a leader of a political party to lead the formation of a government after election.

In Iceland there are two levels of government, national and local. The country splits into approximately 200 local communities at government level where the majority are very small rural communities. Many of these rural communities, or about third, consist of a fishing village and to a varying degree have the rural population in its vicinity⁶⁸. The national government plays a very big role in the governance of the country and was responsible for around 79% of the total government spending in 1995⁶⁹. This reflects well the centralisation that exists in the Icelandic government and the great tendency of the national government to intervene in all possible matters. This centralisation as well as the lack of power of the local governments has resulted in the accumulation of official institutions in the capital area. In the past the government had tried to change this by opening branches of official institutions in bigger towns around the country.

Icelandic politics has for a long time been characterised by “personal service”⁷⁰ with voters, and of great influence of the interest groups in the community⁷¹. The influence of this personal service, and the impact of influencing groups, are in many cases obvious through the lack of long-term strategy and vision of the Icelandic government and the number of ad-hoc decisions and parliamentary exercises. This political environment has been slowly changing over the last ten years or so but the old-style politics is still fairly obvious in many political decisions and actions, for example in

⁶⁸ Magnússon, G.

⁶⁹ Búskapur hins opinbera 1994-95.

⁷⁰ By “personal service” it is meant a favour to the voters.

⁷¹ Kristjánsson, S.; Kristinsson, H. G.

recruitment in official positions⁷². The political environment in Iceland has been quite stable since in most cases the government has seen out their elected four years' period, although there have been some exceptions.

III.7 Conclusions

The Icelandic society has moved fast in this century, from a very simple farming and fishing society with a rather low living standard to a more complicated society with very high living standards. To draw together the major influencing factors, on the economic development in Iceland it is possible to talk about three major factors that is 1) outside conditions, 2) payoff of the fishing grounds, and 3) the economic policy (government influence)⁷³. It can be argued that outside conditions have caused the main turnaround in the Icelandic economic development and put Iceland on the level it has been since. These outside conditions are, for example, WW2 and the Marshal help that followed the war, which boosted the Icelandic economy. This was followed up with an increase in fish catch that continued economic growth in Iceland until around 1970 when other industries started to play a bigger role in the economy.

The management of the Icelandic economy has gone through different phases over the century and to give a fuller picture of the status of Iceland today, a few thoughts about the competitiveness of Iceland will be added. The competitiveness of nations has been defined in many different ways; two common and general definitions are:⁷⁴

1. Competitiveness of a nation is the ability of the nation to produce goods and services which fulfil the demands of the international market with freedom and normal competition.
2. Competitiveness of a nation is its ability to increase the living standards of its citizens permanently.

⁷² Kristjánsson, S.

⁷³ Magnússon, S. M.

⁷⁴ Friðjónsson, Þ., page 91.

In the appraisal of the World Economic Forum which is published in the book "The Global Competitive Report 1996" uses eight main factors to evaluate competitiveness of a nation. These factors are⁷⁵.

1. How open the economy is for international trade
2. The part that the government plays in the economy
3. Efficiency of the financial market
4. Internal strength of the economy
5. The level of technology
6. Qualification of the managers in the companies
7. Flexibility of the labour market
8. Reliability of the judiciary and political systems

Each factor then splits up into more sub-factors but about 2/3 of the weighting is put on factor 1-4 and 1/3 on factors 5- 8. In this appraisal of the World Economic Forum, Iceland is in 27th place in competitiveness and 31st place in economic freedom of 49 nations. It is interesting that Iceland is evaluated much lower according to this method of evaluation than if traditional indices such as GDP and wealth are used⁷⁶. What is most obvious in this evaluation is that the opening of the economy is much more recent in Iceland than in most other countries and the government influences are still too much in areas like banking, communication and power supply⁷⁷. Other factors that influence the Icelandic economy are due to its size and the lack of competition that can arise in such a small economy where few companies compete on the market⁷⁸. An example of this can be taken from transportation to and from Iceland, where one company (Icelandair) dominates charter flights and another company (Eimskip) dominates sea transportation. These two companies are then linked together by over 30% ownership of Eimskip in Icelandair.

Clearly the Icelandic economy has never been closer to an open market driven economy although it still has far to go to be competitive, at least according to the evaluation of the National Forum of Competitiveness. It is also clear that participation in international organisations will keep up pressure to open the economy more but still the politicians and interest

⁷⁵ Friðjónsson, Þ.

⁷⁶ Friðjónsson, Þ.

⁷⁷ Friðjónsson, Þ.

⁷⁸ Árnason, R.

groups in Iceland fight for their interests often against the holistic interest of Iceland and call for protection and support in the form of barriers in the economy. Iceland has build its main strength on the utilisation of the two most important natural resources, that is, the fishing grounds around Iceland and hydroelectric energy. The main weaknesses are that the economy has in many ways been stuck in this utilisation of the natural resources to produce raw materials and to build economic growth through increases of the fish catch. With these factors comes the danger that not enough attention has been given to building up an business environment that would make use of the human resources to increase innovation, both in new disciplines and better utilising the resources that we already have.

The people that live in Iceland seem to have a very positive attitude towards innovation and in many ways have the entrepreneur attitude that is needed to push things forward⁷⁹. This is reflected very well, for example, in how quickly people in Iceland implement, or at least buy new techniques. For example only one country (Finland) has a higher percentage of Internet hosts per thousand inhabitants than Iceland in 1996⁸⁰. On the other hand the weakness is that on the organisational side Iceland seems in many ways to be behind other nations with a similar economical status⁸¹. In many ways Icelanders seem not to like working in big organisations and companies tend to be small and often family-run. This small size of companies can often work as a barrier towards the utilisation of modern technology or other factors that are essential in gaining competitiveness today⁸².

To strengthen the competitive status of Iceland today it seems to be crucial that the governments carry on opening up the economy and creating a healthy economic framework for companies and people to work within. In the same way it is necessary for companies to be able to use these changes as well as their resources to strengthen their competitive status and overcome weaknesses.

⁷⁹ Ólafsson, S.

⁸⁰ Network Wizards at <http://www.nw.com/> In July 1996 Iceland had 40.34 Internet hosts per thousand inhabitants while Finland had 54.25 and UK 9.9.

⁸¹ Ólafsson, S.

IV The Icelandic Fish Industry

The aim of this chapter is to give a short but comprehensive overview of the Icelandic fish industry, its development and its structure. The definitions of “fish” and “fishing industry” vary and can range from activities that are directly related to catching and processing fish to technical- or machinery-related activities. In this thesis, the definition of fish industry will focus on catching, farming, processing, exporting and administration connected to the industry.

IV.1 Brief History

From the earliest settlements, the fish and the sea have been important issues for Iceland. It would have been difficult for people to live in Iceland if not for the food supplies that came from the sea⁸³. Up until the 19th century, fishing was mainly a supplement to farming and was done on rowing boats that were owned by farmers and which were mainly operated seasonally according to the farming conditions. This form of fishing started out as “home fishing” which was operated from the farms. Later this form moved towards the establishment of fishing stations that were closer to the best fishing grounds. In the fishing season, people (mainly workers on the farms) then moved from their farm to the fishing station and stayed there over the operation season which lasted from the end of January to the beginning of May. This continued until the latter part of the 19th century. Other fishing seasons were the spring season from the middle of May to the end of June and the autumn season from the end of September to the end of December⁸⁴. During the 17th and 18th centuries Icelanders had to watch other nations fish in Icelandic waters on large deck sail boats while they were fishing in open small rowing boats just a short distance from the coast. They went out in the morning and came onshore the same day.

⁸² Arnbjörnsson, G.

⁸³ Kristjánsson, L., volume 1.

⁸⁴ Kristjánsson, L., volume 4.

It is surprising how late the Icelandic fishing industry started to develop and that the development started because of pressure and influence from foreigners⁸⁵. The development of the Icelandic fishing industry started in 1783 when the Danish King supported experiments in the operation of deck boats in Iceland. However, these experiments met with resistance from conservative Icelanders, mainly farmers, leading to cessation in 1787. It was at the beginning of the 19th century that Icelanders started to operate their own deck boats and in the middle of that century there were 31 deck boats in Iceland. From that point on it is possible to talk about an independent fishing industry, operating on a full year basis in Iceland.

IV.2 Structure and Development

Sigfús Jónson put forward a model of the Icelandic fish industry which presents the main influencing factors and what impact they have on the economy and community (see figure IV.1)⁸⁶.

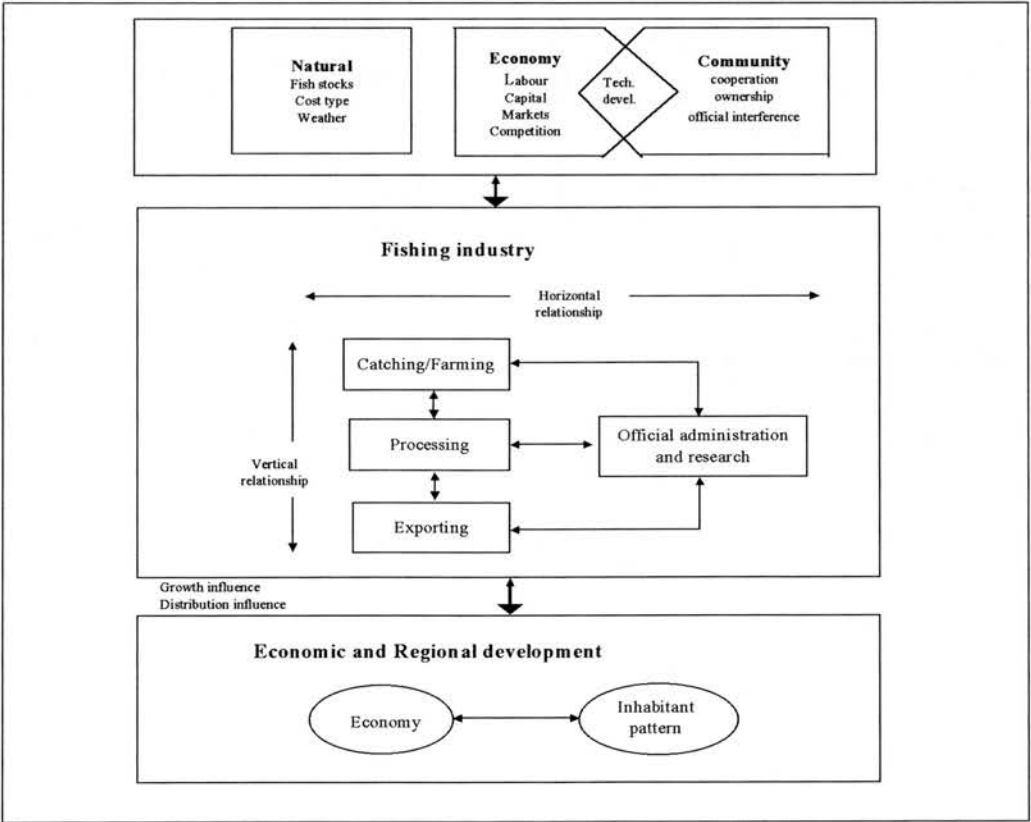


Figure IV.1 Main factors of the fish industry and their impacts⁸⁷.

⁸⁵ Snævarr, S.

⁸⁶ Jónsson, S., page 18.

Figure IV.1 shows that Jónson split the fishing industry into three main factors: catching (fishing sector), processing and exporting. These three factors are influenced by official administration and research. Official administration can both be from the government, in the form of law and regulation, as well as formal administration bodies that the industry itself has established to take care of their own matters. The three main influencing factors are then split into three parts; first the natural factors like fish stocks and weather, secondly the economic factors and thirdly the community factors. To understand these influencing factors it is necessary to look at these factors in Iceland, as well as in countries that are the main competitors for the Icelandic fish industry. Lastly there are the influences of the fish industry on the economy and inhabitation patterns in Iceland. It was made clear in chapter III about the Icelandic economy that the fish industry has great influence on the economic development in Iceland and fluctuations in the Icelandic economy. It is also evident that the fish industry has great influence on the inhabitation patterns in the country, especially in the parts of the country where the fish industry is the main industry and the principal reason for habitation, such as in places like the West Fjord (Vestfjörðum) and the eastern part of Iceland. To understand the Icelandic fish industry and the demands that are made of it, it is necessary to look at all these factors and to understand their impact on the industry. In many cases these factors are not what could be called economical factors; they are more often ad hoc emotional and political, often invisible, factors that follow some tacit principles.

Periods of fast development rather than steady growth have characterised the fish industry. Innovation and development have usually started in the fishing industry and then moved on towards the land processing sector and other related industries and services⁸⁸. In the next section, development in each sector of the fish industry will be looked at briefly to give a more holistic picture of the factors that may influence the industry today.

⁸⁷ Jónsson, S., page 18. The figure been slightly adapted by the author without changing the original format.

⁸⁸ Magnússon, S. M.

IV.2.1 Fishery Sector

In the book “Íslenskur Sjávarútvegur” (*Icelandic Fishing Industry*) Sigfús Jónsson⁸⁹ split the development of the fishing industry into five periods: 1) rowing-boats, 2) sail boats, 3) motorboats and trawlers, 4) innovation-trawlers and Swedish boats, and finally 5) the stern-trawlers. In this section these periods will be used to describe briefly the development in the fishing sector. The author adds one extra period, processing trawlers, which have been developing over the last decade or so. It is interesting to see that until the beginning of the 20th century the majority of improvements and progress in the Icelandic fishing sector were through activities of foreign companies or individuals. It was not until the third decade of the 20th century that Icelanders took the fish industry into their own hands⁸⁹.

IV.2.1.1 Rowing boats 1750-1850

The first period started around the middle of the 18th century when fishing was mainly operated in open rowing boats and on a seasonal basis. Up until the year 1800, fishing was almost only operated in rowing boats.⁹⁰ Rowing boats were widely used until the beginning of the 20th century when engines were first put into such boats. Following this, the use of rowing boats went into a rapid decline.

IV.2.1.2 Sail boats 1850-1905

The second period lasted from the middle of the 19th century until 1905, when deck sailboats became increasingly important in the fishing sector. At the turn of the 20th century the number of deck boats was 150.

IV.2.1.3 Motor boats and trawlers 1905 - 1945

The third period started in 1902 when the first engine was put into a boat and in 1905 when the first trawler came to Iceland. From this point on, development in the fishing sector was fast, and the catching of demersal species, which had been the most important in Iceland, doubled from 1905

⁸⁹ Snævarr, S.

⁹⁰ Jónsson, S.

to the beginning of WW1, or from 40,000 tons to 100,000 tons. In the 1920s, the catch went to 340,000 tons when Icelanders started to catch saithe, which up to that point had not been utilised. Employment in the fishing and processing sector reached its peak in 1930 when 23% of the total work force were working in both these sectors and over 15% of the total work force in the fishing sector. In the 1930s, a problem period appeared due to sales problems on foreign markets and the decreased catching of demersal species, especially cod and haddock, relative to a simultaneous increase in the catching of herring. During WW2, the circumstances of the fish industry changed because the traditional market for products closed or was difficult to supply. As a result of this, the export of fresh fish to Britain increased and prices went up. During WW2 the fishery sector was very profitable and able to put money in saving funds to prepare replacements of fishing vessels that were getting old and out of date⁹¹.

IV.2.1.4 Innovation-trawlers and Swedish boats 1945 - 1970

At the beginning of this period, the Icelandic government made a contract to build new trawlers to renew the ageing fleet. These trawlers got the name innovation-trawlers to refer to the impact they were supposed to have on the industry. In the same way the government made a contract to build boats in Sweden to renew the boat fleet. Between 1945 and 1952 the fleet increased but during the latter part of the period, i.e. post-1955, the catching of demersal species stock decreased. Between 1960–1966 operation of trawlers became difficult and their numbers declined from 47 to 22⁹². An increase catch of herring made up part of the loss of the catch of demersal species, but mainly for the boats rather than the trawlers. The catch of herring was great in the years from 1960-67, which meant that herring almost disappeared from the fishing ground due to over-fishing.

⁹¹ Jónsson, S.

⁹² Jónsson, S.

IV.2.1.5 Stern-trawlers 1970 - 1985

From around 1970 onwards, the trawler fleet was renewed and stern-trawlers were bought. Their introduction was so well received that their numbers increased very rapidly and the government supported this development by offering good funding. The government used this as a regional development policy, to enable companies in small villages to buy stern-trawlers, which would increase the stability of these operations, increase employment and reduce the drain of people from the rural areas. This meant that, as well as an increase in the catch, the number of trawlers increased from 22 in 1970 to 54 in 1974 and to 103 in 1983. After the collapse of the herring catch in 1967 the boat fleet started to concentrate more on other species such as capelin and shrimp, as well as catching demersal species like cod. In 1982 and 1991 the catch of capelin collapsed; although it had been very important for the boat fleet, the catching of capelin has always fluctuated. After 1970 the fishing fleet increased the range of fish caught, including species that had not been as important previously, for example greenland halibut, capelin, and ocean redfish. After 1982 the total catch fell because of over-fishing and declining fish stocks. This decline has continued in all major species until 1997, when some evidence showed increase in fish stocks and quotas.

IV.2.1.6 Processing-trawlers 1983 - 1997

In 1983 processing at sea started in some real quantities when mainly trawlers and bigger boats began to be adapted. This processing includes mainly freezing the fish either whole, headed or filleted, trimming the fish and freezing it in blocks. The output of the sea processing vessels was 24 thousand tons in 1983 and went up to 155 thousand tons in 1994 but has declined a little since then, mainly because of declined fish stocks. In the last five years or so, new trawlers and big boats with processing facilities have been bought and have made it possible for the fleet to fish on international fishing grounds which in some cases are without quotas and control. In 1995, the demersal species made up 81% of sea frozen products,

and shrimp 19%. During the period from 1983 onwards these percentages have fluctuated from 80-90% for demersal and 10-20% for shrimp.

IV.2.2 Fish Farming

Fish farming started to some extent in Iceland in the 1970s, mainly with salmon. Export of fresh-farmed salmon started around 1980. The production of farmed fish has gone from 3 tons in 1983 to around 3,000 tons in 1993 and was still around that in 1997⁹³. Around 1980 the Icelandic government offered support and favourable loans to encourage fish farming which they thought would be very positive for the Icelandic economy and would support more economic diversity. When farmed salmon from Iceland was put on the market the price was falling due to increased production in countries like Norway and Scotland. In addition to this, countries that had been farming much longer had lower price, as they had managed to lower the production costs. Conditions for fish farming are in many cases more difficult in Iceland than in other countries due to the cold sea. The optimism concerning fish farming thus ended with disappointment and difficulties for companies that had started in farming. This bad experience has in many ways been a barrier for further development of fish farming in Iceland, where favourable conditions, such as the geothermal water, could be utilised to a greater extent. However, this is slowly changing and fish farming, such as river trout farming, has increased. In addition, three companies now operate as experimental companies, one in farming halibut, another in European sea bass and the third in abalone.

Table IV.1 presents the production of slaughtered fish from the year 1992 to 1995.

Production of fish farming 1992 - 1995				
	1992 ton⁹⁴	1993 ton	1994 ton	1995 ton
Salmon (From all farming methods)	2.585	2.844	2.896	2.880
Trout (all species)	399	566	574	860
Total	2.984	3.410	3.470	3.740

Table IV.1 Production of fish farming 1992 - 1995⁹⁵

⁹³ Helgason, St. S.

⁹⁴ The volume is ungutted fish.

Table IV.1 shows that there has been over 100% increase in trout farming from 1992 to 1995 and a slow growth in salmon farming at the same time. Although fish farming does not play a major part in the Icelandic fish industry, it represents around 22% of global fisheries production in the world in 1996 and increases its share every year (was 8% in 1984)⁹⁶. Hence, Icelandic fish is in increased competition with farmed fish from other nations.

IV.2.3 Fisheries control and management

Fishing management and control can be split up into three important periods: (1) when the Icelandic government increased the Icelandic fisheries' limits during the period 1952-75, (2) in 1983 when quotas were placed on catching of the most important species and (3) in 1990, when quotas were put on all species and boats and individual transferable quotas were introduced on all species.

IV.2.3.1 Icelandic economic exclusive zone

An extension of the fisheries' jurisdiction started in 1952 when its limits were extended from 3 to 4 miles and from 4 - 12 miles in 1958. In 1972 the Icelandic government decided, unilaterally to other nations, to extend the jurisdiction from 12 to 50 miles and again in 1975 from 50 - 200 miles. These extensions were made because of fast declines in the fish stocks and over-fishing in the fishing grounds around Iceland. Between 1950 and 1974 foreign fishing vessels caught on average of 360.000 thousand tons of demersal species in the sea around Iceland, which is a similar catch to that of the Icelandic fleet for demersal species⁹⁷. This foreign fleet was mainly from Britain (about 60%) and West Germany (30%)⁹⁸. After each of the four extensions Britain imposed a landing ban on Icelandic ships; West Germany imposed this after the last two extensions. The third conflict in 1972 also had an effect on the Icelandic fish industry; Protocol 6 in the EEC

⁹⁵ Útvegur 1995.

⁹⁶ Grainger, R.

⁹⁷ Jónsson, S.

⁹⁸ Bjarnason, A.

agreement meant that, without reaching a satisfactory agreement with EEC countries, Iceland would not enjoy specific reductions on import duties on fish to EEC countries. This sanction lasted from 1972 to 1976 when Iceland reached an agreement over the 200 miles limit. Since 1976 fishing of foreign ships in Icelandic waters has been very limited and plays no important role in the total catch.

IV.2.3.2 The Quota system

The next aspect of fishing control that is worth mentioning is the quota system. It was introduced in 1983, with quotas on important species, either in the form of quantities or limitations regarding the number of days that ships could fish each year. Before 1983 a quota system had been introduced in the herring fisheries in 1975 and in 1980 this was extended to the fishing of capelin. The main pressure for introducing the quota system was declining fish stocks first the collapse of the herring stock and, later on the foreseeable collapse of the capelin stock without preventive measures. The same can be said about the demersal species before 1983 where the stock had been declining due to overfishing. Hannesson has pointed out that the ownership of quotas involves the right to catch the fish but not ownership of the fish stock⁹⁹. Due to this it is claimed that the quota does not mean the ownership of the fish but rather the right to catch the fish.

From the beginning of the quota system the quota has been bound to the fishing vessels. In the first years of the quota system, two main systems were active. First, the quantities quota where the fishing vessels were assigned certain quantities that they could catch. Then there was the fishing effort system that allowed the vessels to fish for certain number of days over the year. Later the fishing effort system was abolished for all vessels except for boats under 10 tons that could choose between systems. In 1995 the fishing law was modified slightly so it would also cover boats under 10 tons, which before had been exempt from the quantity quota¹⁰⁰. Still, boats under 10 tons can be included in the fishing effort system which allows

⁹⁹ Hannesson, R.

¹⁰⁰ Útvegur 1995.

them to fish for a limited number of days per year (around 23 days per year in the year 2000).

IV.2.3.3 Individual transferable quota (ITQ)

The law in relation to fishing was amended in 1990 in order to make the quota system more effective rather than responding to declining fish stocks or overfishing as almost all law concerning the quota had previously attempted. According to law 1, no. 38, May 15, 1990 no one can catch fish inside the Icelandic economic zone without permission from the Ministry of Fisheries, and licences are given for one year at a time¹⁰¹. Due to this law, all major fisheries inside the Icelandic economic zone operate according to a uniform system with transferable quotas in all species and fisheries. Hence, nearly all fishing vessels have individual transferable quotas (abbreviated ITQ), allowing ship owners to buy or sell quotas between ships. As has been pointed out earlier, the ITQ grants the right to catch the fish but not the ownership of the fish stock¹⁰². In that way, the ITQ permits the owners of the fishing vessel to sell the right to catch the fish. However, there are limitations to the transferability of the ITQ that could affect the structure of the fisheries sectors. Firstly it is exclusively owners of fishing vessels with a valid fishing licence that can hold quotas. Secondly, the holders of quotas must catch at least 50 percent of their quotas every second year to maintain the quota share. The third restriction is the geographical restriction to the ITQ system where the local authorities and respective fisheries unions in local geographical regions can block the transfer of annual quotas between regions. On the other hand, annual vessel quotas are freely transferable between fishing vessels within the same region. Runólfsson and Árnason point out that it is rare in practice, that transfers of quotas between geographical regions are blocked¹⁰³.

Runólfsson and Árnason claim that *“The fishing industry is a major determinant of personal incomes and income distribution and, in many parts*

¹⁰¹ Fisheries Management Act No. 38/1990.

¹⁰² Hannesson, R.

¹⁰³ Runólfsson, B. & Árnason, R., 1996.

*of Iceland, the fishing industry is virtually the only basis for economic activity. Anything that affects the fishing industry, therefore, has a regional impact that often has very potent political repercussions. As a result, the fisheries management is a major topic of public discussion and has great influence on the formulation of Icelandic economic and regional policy*¹⁰⁴.

Consequently it is no surprise that the transferability of the quotas has been criticised as a weakness where it would lead to concentration of quota holdings within a few big companies. This will leave the smaller companies, many located in the rural areas, without quotas and employment. Runólfsson and Árnason point out that it is in the nature of any fisheries management system to increase the efficiency and profitability of the fisheries which will at least partly be done through a smaller fishing fleet¹⁰⁵. Decreasing the total allocation of quotas causes pressure in the fishing sector to increase concentration by merger or acquisition. This can be seen when in 1992 the twenty biggest quota holders had a 36% share of the total quota but in March 2001 the share had increased to 59% of the total quota¹⁰⁶. This demonstrates that there has been concentration in the fishery sector with companies getting bigger. This concentration needs to be looked at in the light of the high proportion of vertical integration between the processing and fisheries sectors where vertical integration is almost a norm in the industry. Hence, this concentration in the fisheries sector also applies in the processing sector.

It is clear that the ITQ system and the concentration that has occurred in the industry cause a tension between the economic and political views aimed at regional development. The concentration and the ITQ system in some way support a healthy industry where the industry can adjust to changes in the business environment by moving or selling quotas between companies. On the other hand, it is the regional development that suffers when companies that have been big employers in the region are bought and the fishing vessels

¹⁰⁴ Runólfsson, B. & Árnason, R., page 1, 1996.

¹⁰⁵ Runólfsson, B. & Árnason, R., 1996.

¹⁰⁶ Haraldsson, L. H.

and quotas are moved away, leaving the small villages almost without employment.

Another aspect of the critique of the ITQ system is the value bound in the quotas and the fact that owners of companies or fishing vessels can sell their share in companies where biggest part of the price is paid for the quota. It is evident that this has made it possible for some owners of companies in the fisheries sector to leave the industry with a good profit. On the other hand it can be argued that without this price for the quota it would be very difficult to leave the industry without losing a considerable amount or even going bankrupt. Despite this, the holders of the quotas have only paid a very small price to the community for the right to fish and, therefore critics have claimed that the owners of the fishing companies have been “given” the quotas which they then can sell at high prices. In the beginning, the annual quota was issued by the Ministry of Fisheries free of charge. In 1990 this changed in such a way that now the Ministry collects fees for the annual quota to cover the cost of monitoring and enforcing the ITQ system¹⁰⁷. The fee only covers a very small amount compared to the price of the quotas on the market. All this has caused disagreement over the ITQ system and over the effect it has had on developments in the fishing industry as well as regional development.

In evaluating the quota system it is necessary to look at the previously described high degree of vertical integration that has taken place between the processing and the fishing sectors. Without this vertical integration between these two sectors it can be suggested that the quota system, and especially the fact that the quota is bound to the fishing vessels, could seriously affect the power balance in the industry. Quotas that are bound to the fishing vessels put the owner of the vessels in a very powerful position in bargaining against the processing sector about prices and other matters concerning business dealings between the sectors. Hence, it is claimed here that the high degree of vertical integration has minimised this proposed negative effect of the quota system and is one of the prime reasons for the success of the quota system in Iceland.

The current situation is that all boats have quantity quotas (except for boats under 10 tons that remain within the fishing effort quota system) for all species, and permission to fish for one year, the so called “fishing year” which starts on the 1st of September and ends on the 31st of August.

IV.2.4 Fishing fleet and catch

To get a better overview of the fishery sector today, it is helpful to look at three factors; (1) size and structure of the fleet, (2) the catch, and (3) the disposal of the catch.

Fishing fleet in 1997						
Type of fishing vessels	Size in GRT ¹⁰⁸	Number of ships	GRT	% of total GRT	% of total catch	% of total value
Seasonal boats	0-12	313	2,420	1.9	1.8	4.9
Multipurpose vessels	13-50	123	3,052	2.5	2.7	7.8
-----	51-110	83	6,487	5.2	2.3	6.5
-----	110-200	77	12,165	9.7	4.1	11.5
Multip and specialised	201-500	62	19,165	15.3	37.6	14.6
purse-seiner vessels	501-800	12	8,054	6.5	22.7	6.4
-----	>800	5	5,474	4.4	13.8	3.6
Trawlers	0-500	63	24,625	19.7	7.5	17.2
	>500	52	43,454	34.8	7.5	27.5
Total		790	124,896	100.0	100	100,0

Table IV.2 The fleet, size and catch 1997¹⁰⁹.

Table IV.2 shows that the trawlers bring ashore the most valuable catch, or almost 47% of the total value, while the multipurpose boats bring the most volume, mainly due to the capelin catch, the majority of which is reduced into fish meal. From 1975 the GRT (Gross registered tonnage) of the boats from 0 to 500 GRT has declined by about 28%. The boats over 500 GRT have increased in GRT by about 7% and the trawler have increased in GRT by about 21% and the trawler over 500 GRT have increased in GRT by about 18%. This means that the number of ships in the fleet is declining and the ships are getting bigger. This development has been rapid since 1985, especially with these big trawlers and boats with processing facilities. This development has mainly affected the trawler group and bigger boats. Table

¹⁰⁷ Runólfsson, B. & Árnason, R., 1996.

¹⁰⁸ GRT, stands for Gross registered tonnage.

¹⁰⁹ Útvegur 1997, tables 4 and 20a.

IV.3 presents the main species and fishing gear of each of the groups of the fishing fleet.

Main species and fishing gears			
Type of fishing vessels	Size in GRT	Main species	Main fishing gear
Seasonal boats	0-12	Demersal	Handline,
Multipurpose vessels	13-50	"	Longline, Gillnet
-----	51-110	Demersal., Herring.	Longline, Gillnet
-----	110-200	Shell fish	purse-seine, trawl
Multip and specialised	201-500	Demersal., Herring./	Trawl
Purse-seiner vessels	501-800	Shell fish , Capelin	purse-seine
-----	>800	"	"
Trawlers	0-500	Demersal., Shrimp	Trawl both
	>500	"	bottom and flow

Table IV.3 The fleet, main species and fishing gear¹¹⁰.

Demersal species are the most important fish species in the fishery sector with over 54% of the total value of landed fish (see Table IV.4). On the other hand pelagic species, mainly capelin, stand for over 74% of the quantity of landed fish. However capelin fishing is built on quantity where a large part of it goes into fishmeal production, although an increasing proportion is frozen.

Total catch 1997				
	Value in thousand. isl.kr.	Percent of total value	Quantity in thousands ton	Percent of total quantity
Demersal species	30,353,103	53.8	430,399	19.6
Flatfish	5,866,007	10.4	46,905	2.1
Pelagic fish	10,176,032	18.0	1,620,787	73.7
Molluscs and Crustaceans	10,025,228	17.7	99,824	4.5
Other	46,683	0.1	1,096	0.1
Total	56,467,053	100.0	2,199,011	100.0

Table IV.4 Total catches 1997¹¹¹.

To get a better picture of individual species inside each group, the ten most important species in value are presented in Table IV.5. In 1997 Cod was less than half of the quantity in 1981 when it was in its maximum. Cod still is the most important species in the Icelandic fishery industry and stands for 28% of the total value of landed fish. In later years shrimp has become the second most important species and sea frozen product. As an example of the fluctuation in the Icelandic fish industry, shrimp was around 41% of the

¹¹⁰ Útvegur 1995.

¹¹¹ Útvegur 1997, table 29.

quantity in 1995 but dropped to around 17% in 1997. In these two years the catch of shrimps has declined by 24% of the total catch, meanwhile the catch of cod has increased by 6%, from 22% in 1995 to 28% in 1997.

Most important species in 1997				
Species	Value	%	Ton	%
Cod	15,579,987	27.59%	208,622	9.49%
Shrimp	9,341,083	16.54%	82,627	3.76%
Capelin	7,669,095	13.58%	1,313,624	59.74%
Redfish	7,644,557	13.54%	109,583	4.98%
Haddock	3,539,598	6.27%	43,248	1.97%
Greenland Halibut	3,376,939	5.98%	18,630	0.85%
Herring	2,219,987	3.93%	291,117	13.24%
Saithe	1,728,654	3.06%	36,546	1.66%
Plaice	1,143,309	2.02%	10,544	0.48%
Catfish	792,785	1.40%	11,666	0.53%
Total	53,035,994	93.92%	2,126,207	96.69%

Table IV.5 Ten most important species in fish catch 1997¹¹².

Most of the volume goes to meal production, where capelin is the main species, as well as herring. Although most of the volume (48%) goes to meal production, meals stood for only about 16.4% of the total export value of fish products in 1997¹¹³. The most valuable method is freezing; but in 1997 land freezing took 15% of the catch and sea freezing 8.6%, but (together 23.6% of the total catch) they stood for around 55% of the export value of fish from Iceland¹¹⁴.

IV.2.5 Processing Sector

In the past the main aim of most processing methods was to expand the lifetime of the fish so it could be kept under the primitive conditions of the time. Developments in fish processing have principally followed the development of the fishing sector. Fish processing was connected with the boat owners, usually farmers who processed their own catch. With the emergence of bigger boats and individual boat owners (who were not farmers), operation on a whole year basis started around the middle of the 19th century. From this time it is possible to talk about a significant fish industry, both in terms of fishing and production. However, it was not until

¹¹² Útvegur 1997, table 29.

¹¹³ Útvegur 1997.

¹¹⁴ Útvegur 1997.

around 1930 that individual processing companies emerged that were not bound to the operation of fishing vessels¹¹⁵. After this it is possible to talk about an independent fish processing industry, although the link between fishing and processing is obvious. Today most of the processing companies operate their own fishing vessels to take care of supplies for their production.

The oldest processing method for fish in Iceland was to dry the fish to make the so-called stockfish, which is the oldest exported fish product from Iceland. In the middle of the 19th century salted fish took over as the main processing method, until the closing of the main market in Spain during the Civil War in the middle of the 1930s. After that, selling of fresh unprocessed fish increased considerably, and between 1930 and 1950 freezing took over as the main processing method in the industry, and has kept its position ever since.

IV.2.5.1 Production methods

Production methods for fish in Iceland can in the simplest way be split into six main groups: 1) freezing, 2) salting, 3) drying, 4) fresh, 5) meal and oil and 6) canned. In export reports unprocessed fish exported on ice is counted as fresh although it gets no treatment or processing in Iceland. As can be seen from Figure IV-2 which shows the percentage of value each year that is produced, there is a fluctuation in and between each production method. Many factors influence the choice of production methods, for example market condition, exchange rate, quantity and quality of the catch and the production capability. Another factor influencing the choice is flexibility of the production companies; the majority of the bigger companies are capable of switching between processing methods when, for example, market condition are favourable or the quantity of catch is too much for just one processing method.

¹¹⁵ Jónsson, S.

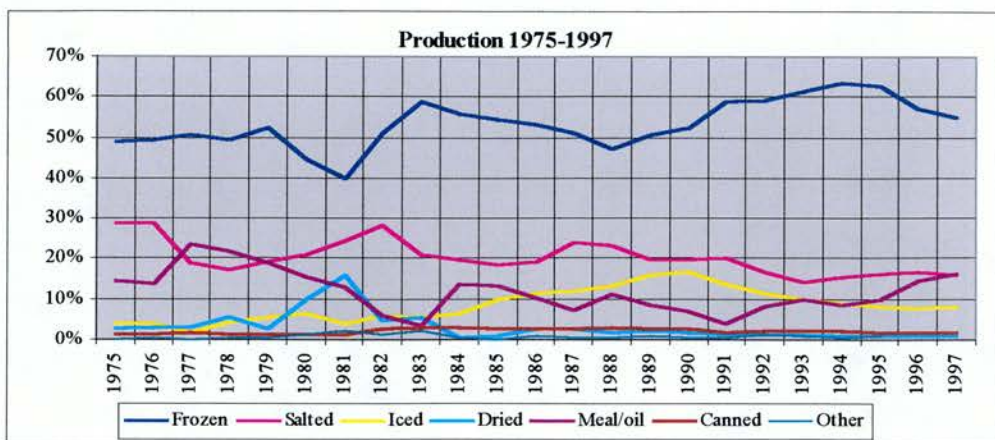


Figure IV.2 Production the fish processing 1975-1997¹¹⁶

The next sub-section provides a short description of each of these processing methods and their development in Iceland, starting with drying of fish, the oldest method.

IV.2.5.1.1 Drying (Stockfish)

The history of stockfish production can be traced back to the year 1200 and the first written source about export to the year 1340¹¹⁷. Stockfish production was the most common processing method for fish in Iceland until the middle of the 19th century. Stockfish production was almost zero at the beginning of this century but around 1950 it became important again as the catch of demersal species increased and a market for it opened in Africa. In this century stockfish production reached its peak in 1981 when it stood for around 16% of the total value of fish production from Iceland, which was mainly exported to Nigeria. However, the market there collapsed the year after due to one of many revolutions in the country. After that the market in Nigeria has mainly been for cheap by-products like dried cod heads and fish bone. Over the last decade stockfish production has fluctuated from 0.71% to 2.68% of the total value of the fish production, with the main market for quality stockfish being Italy, and for cheaper production, Nigeria. Traditional stockfish production is usually a by-product for companies and demands neither a lot of technology, equipment nor capital. Very few companies have stockfish production as their main

¹¹⁶ Útvegur 1997, table 34.

¹¹⁷ Kristjánsson, L., volume 4.

activity, although a few companies located near geothermal heat sources have used this natural resource for drying cod heads, bones and fish cuttings as their main activities.

IV.2.5.1.2 Salting

Salting of fish was not common until the beginning of the 19th century although sources report that fish was salted in Iceland from around 1624-30. Between 1820-40 salting became increasingly important in the southern part of Iceland but until 1870 most of the fish in the north and east of the country was processed into stockfish¹¹⁸. After this, at the end of the 19th century, almost all the catch was salted due to increased knowledge of the processing method, good access to salt and favourable market conditions. The main markets for salted fish (called Bacallo) have traditionally been in southern Mediterranean countries like Italy, Spain, Portugal and Greece. During the Civil War in Spain and WW2, an increase in freezing meant that salting lost its place as one of the main production methods for fish in Iceland between 1930-40, but salted fish has always been an important fish product. From 1975 to 1997 it has fluctuated between 14.34% - 28.86% of the total value of exported fish compared to 16.0% in 1997. Salt fish production from demersal species demands neither great equipment nor technology so, even today, boat owners often process their own catch with their families. Thus companies using salting are characterised mainly by small ones with 1-5 employees, although there are bigger companies that have implemented much more technology to the production in the last decade. Salt fish production is also often a by-product or second product for companies. The main species for salting are demersal, mainly cod and herring, which are salted into casks into which other species are often added.

IV.2.5.1.3 Freezing

Freezing can be split into two parts, traditional land freezing and freezing at sea, which has been increasing over the last two decades. Freezing of fish started in Iceland in the 1930s and increased dramatically over the period 1940-50 and again in the 1960s when Great Britain put a landing ban on

¹¹⁸ Jónsson, S.

Icelandic fishing vessels due to a fishing dispute which put pressure on companies to increase their processing capacity. Freezing demands much more technology and capital than both drying and salting, so companies tend to be bigger and have freezing as their core processing method, although many companies also have the opportunity to use some other processing methods like salting. Freezing has accounted for about 50% of the total value of fish production for the last two decades, or from 38.9% in 1981, when a large proportion of fish caught went into stockfish production, up to 63.6 % in 1994. Freezing on land has, for the last decade or so, faced increased difficulties in operation and competition from processing trawlers which process the fish on board. In sea freezing the fish is frozen very fresh or usually within 24 hours of catching and the processing trawlers operate 24 hours per day in 20- to 30- day cruises. This means that their output on capital is much higher than for land freezing and the fish is fresher. If the Pelagic species are excluded, around 32% of the total catch was frozen at sea in 1997, including where 29.6% of demersal species, 36.0% of flatfish species and 50.3% of the total catch of shrimp¹¹⁹. Rarely do the processing trawlers have the facilities to utilise the cuttings and bones from the fish, nor do they have the facilities to cut or trim the fish as is possible in land processing. This means that processing at sea is much simpler than land processing and does not offer as much opportunity for value adding through more work. This leads to the product frozen at sea being much closer to a raw material for further processing, which is usually done abroad.

IV.2.5.1.4 Meal and oil

The production of fishmeal and oil depends heavily on the catch of capelin and herring, which are the most important species both for fishmeal as well as oil. About 92.3% of the capelin catch and around 81.3% of the herring catch in 1997 went into fishmeal and oil production¹²⁰. Due to an increased catch of herring in the summer time (*Íslandsild/Iceland's herring*) the percentage of the catch that goes into meal production has again increased,

¹¹⁹ Útvegur 1997.

¹²⁰ Útvegur 1997.

from nearly 56% in 1991 to around 81.3% in 1997¹²¹. Another aspect of the fishmeal and oil production industry is the utilisation of fish bones and cuttings from the processing companies, but with an increase in sea processing this production has declined over the last years. Another sector in this industry is the utilisation of fish products such as fish liver for liver oil for human consumption, both for domestic consumption as well as for export.

Companies in the fishmeal and oil sector are in most cases separated from other processing companies or the fishing sector. It is common though that other fish companies own a share in fishmeal companies near their processing plants or have small melting facilities attached to their production.

Production in this sector fluctuates greatly, mainly due to fluctuations in the catch of capelin and herring both in Iceland as well as in competing countries like Canada and Norway. Fishmeal and oil production has fluctuated from around 3% of the total export value of fish product from Iceland to 25%¹²².

IV.2.5.1.5 Canning and preserving

Canning has a long history in Iceland but preserving is much newer and began around 1955. Herring and shrimp are the most important species but this sector also utilises lumpfish, cod-roes and cod-liver. Most of the production in this sector is exported in packaging that is ready for sale and consumption. At a glance the canning and preserving sector is much closer to the consumption market than most of the rest of the fish production industry in Iceland. In 1997, production from this sector stood at around 1.9% of the export value of fish product in Iceland¹²³.

IV.2.5.1.6 Fresh (Iced)

The export or sailing with fresh iced fish did not start until WW1, although foreign fishing vessels had been fishing in Icelandic waters and sailing back

¹²¹ Útvegur 1991.

¹²² Snævarr, S.

¹²³ Útvegur 1997.

home with their catch for a much longer time¹²⁴. Sailing with fresh fish has fluctuated greatly over its history, depending on catch and market conditions. With improvements in transportation, export of fresh fish in containers became increasingly common in the 1980s. Export of fresh fish in containers opened a new option for smaller boats that could not sail themselves with the fish to foreign auction markets; they could share containers and send it to the market that way. In 1997 around 5.9% of the catch of demersal species was exported in containers and around 5.9% of the catch of demersal species was exported by the fishing vessels themselves to foreign auction markets¹²⁵.

IV.2.6 Export Sector

After the monopoly of the Danish merchants ended in 1787 the licences for export from Iceland was bound to Danish citizen all until 1855 when it was given free. The export of fish from Iceland was therefore rather free with minimum government interference, with the exception of the WW1 period up until 1930¹²⁶. From 1900 to 1930 the most important export of fish from Iceland was cod, either salted or whole on ice, and fish liver oil¹²⁷. Most of the export of salted fish during this period went through individual fish merchants who bought the fish from small producers and sold to markets in Mediterranean countries, mainly Spain and Italy¹²⁸. After 1930 a period of government interference in export matters and oligopoly took over, until around 1980 when exports increased, along with competition in exporting. This led to liberation of exports in the late 1980s and early 1990s. This discussion about the export sector will be divided into these two periods; that is, firstly the government interference and oligopoly during the period 1930 - 1980, and secondly post- 1980, which was characterised by increased competition and freedom. These periods are more or less in coherence with

¹²⁴ Snævarr, S.

¹²⁵ Útvegur 1997.

¹²⁶ Jónsson, S.

¹²⁷ Bjarnason, A.

¹²⁸ Bjarnason, A.

the general economic development in Iceland as previously discussed in Chapter III.

IV.2.6.1 Government interference and oligopoly 1930 - 1987

In the 1930s the export of salted fish became increasingly difficult mainly due to the “Great Depression” and huge overproduction of salted fish in the world¹²⁹. These difficulties induced lower prices and chaotic situations in the main markets where commission agents controlled almost everything and the producers or fish merchants underbid each other in the hope of selling their products. During this period, five companies took care of most of the export of salted cod from Iceland. Due to the bad conditions on the markets, rapid underbidding and badly organised selling the commercial banks of the Icelandic fish and fishery companies pressed for more cooperation in the export of fish¹³⁰. This ended in July 1932 when the three biggest export companies, banks and companies in the fish industry established Sölusamtök Íslenskra Fiskframleiðenda (Union of Icelandic Fish Producers), abbreviated UIFP. In December 1932 the Icelandic government granted UIFP an almost entire monopoly on exporting salted cod from Iceland with temporary law. This law strengthened the organisation in place where it would otherwise have been difficult to get all the companies in the production and selling of salted fish to work together in one sales organisation. Since the expiration of this temporary law the Ministry of Foreign Affairs granted permission to export fish on a year-to-year basis. UIFP was the first export organisation established in Iceland in the ownership of companies in the fishing industry. It can be said that with its establishment and by granting the organisation a monopoly, the Icelandic government had started its massive involvement in the organisation of the export of fish from Iceland.

The next organisation in the Icelandic fish industry was the establishment of Sildarútvegsnefnd (Icelandic Herring Board), abbreviated IHB, in 1934. IHB’s initial role was to supervise and exercise an overall control on the

¹²⁹ Valdimarsson, U. V. & Bjarnason, H.

¹³⁰ Valdimarsson, U. V. & Bjarnason, H.

catching, processing and exporting of herring in Iceland. However, it was not until 1945 that IHB was granted a monopoly in exporting salted herring from Iceland¹³¹. IHB is a private foundation with some of its board members elected by Alþingi (parliament) and others appointed by the Ministry of Fishery.

Another involvement of the government in the 1930s was the establishment of Fiskimálanefnd, which was an official authority, which aimed to support innovation in the fish industry as well as supporting the establishment of freezing plants around the country. A few years later the Fiskimálanefnd (Fish affairs committee) got the unofficial authority as an overall government body in all matters concerning the fish industry in Iceland. After the establishment of UIFP and the controversy over how the fish export should be organised in Iceland, the Fiskimálanefnd was granted a monopoly of exporting frozen fish from Iceland. Fiskimálanefnd put pressure on the freezing plants, which they had supported, to sell their products through them, and exercised its authority by denying granting companies an export licence.¹³²

In the New Year 1940/41 companies in the freezing industry, which were inside the Samband Íslenskra Samvinnufélaga (Federation of Icelandic Co-operatives), abbreviated SÍS, handed their sale activities over to the Federation from Fiskimálanefnd. Then, in 1942, the privately owned companies in the freezing sector established their own sales organization Sölumiðstöð Hraðfrysithúsanna (Icelandic Freezing Plants Corporation), abbreviated IFPC. IFPC gradually took over sales on behalf of their companies from the Fiskimálanefnd, which had taken care of sales for the IFPC in their first months, and much of the staff followed to IFPC from the Fiskimálanefnd¹³³.

Partly due to the conditions that the government put on the establishment of sales organisations in the fish industry and granting export licences, the two organisations (IFPC and UIFP) that were established by private companies

¹³¹ Bjarnason, A.

¹³² Hannibalsson, Ó. & Einarsson, H.

¹³³ Hannibalsson, Ó. & Einarsson, H.

operated on a Co-operative basis. SÍS was run before on a Co-operative basis but all three companies, that is SÍS, UIFP and IFPC, were operated as non-profit organisations, which returned their profits to their members through lower commission on sales. As outlined earlier IHB was operated as a private foundation, getting its revenue through commission on sales and imported supplies needed for the herring production¹³⁴.

After 1940 the Icelandic government controlled exports from Iceland through the granting of export licensing by the Ministry of Foreign Affairs. The main aim of the government during this time was to minimize internal competition and the underbidding of companies exporting fish from Iceland. To ensure this the government granted very few companies export licences to the most important markets, blocking internal competition between companies in the fish industry and guaranteeing oligopoly. In general terms this meant that the organisation of the export of salted and frozen demersal species to these markets was as follows:

- UIFP had an almost monopoly of the export of salted demersal fish to the Mediterranean countries until 1st of January 1993.
- IFPC and SÍS (and later IS its successor) had an almost duopoly for frozen fish on the US market until 1987.
- In the former Soviet Union, IFPC and SÍS (and later IS) had also duopoly until the market closed after the collapse of the Union in 1991.
- Export to Western Europe was much more liberated for frozen fish than in the US and the Soviet Union, and in the 1960s companies other than IFPC and SÍS started exporting to these countries¹³⁵.

In the fish meal and oil sector the government was heavily involved in its export by its ownership of the biggest company in that sector, Sildarvinnsla Ríkisins (The Icelandic State Factory), abbreviated SR, until 1994. Export in the fishmeal and oil sector has always been much more decentralized than in the other sectors of the fish industry and not under as much control from the government¹³⁶.

In canning and preserving the government was also involved; it formed a sales organisation with processing companies, called, Sölustofnun

¹³⁴ Bjarnason, A.

¹³⁵ Bjarnason, A.

¹³⁶ Bjarnason, A.

Lagmetisins (Icelandic Waters), abbreviated SL, in early 1970 to take care of producers' sale activities. The canning sector is dominated by 3-4 producers that account for around 90% of the total export¹³⁷. Therefore in 1991, when some of these big companies decided to take care of their own sales activities, SL lost its share of export and in 1993 it merged with one producer under the name Icelandic Waters.

This period 1930 - 1980 is characterised by oligopoly of the big sale organisations, IFPC, SÍS, UIFP, IHB and later SL, which dominated exports from Iceland. In 1982 IFPC, SÍS and UIFP exported 71.5% of the total export of fish product from Iceland, and if IHB and SL are added to that the share of the total export is 77.0%¹³⁸. From here these four companies IFPC, SÍS/IS, UIFP and IHB will be called Principal Marketing Companies, abbreviated PMCs. Although the government limited export licensing, a number of new firms entered the export sector during this period, but relatively few managed to stay in the export business for more than a few years¹³⁹.

IV.2.6.2 Competition and increased freedom 1980 -1999

With increased fish catch and more diversity of the markets for fish, export of fish increased heavily during the period after 1980. As a result an increased number of small companies entered the export sector, especially between 1983 – 88, leading to increased competition especially in the export of frozen fish. This can be traced to the increased importance of the EEC market for frozen fish, on account of a decline in the US market. As can be seen from Figure IV.3, the percentage of the total export of fish product from Iceland to the US market declined from around 48% in 1975 to around 12 - 18% in the 90s. At the same time, the EES market increased its share of the total export from around 39% in 1975 to around 64% - 74% in the 90s.

¹³⁷ Bjarnason, A.

¹³⁸ Bjarnason, A.

¹³⁹ Bjarnason, A.



Figure IV.3 Markets for export of fish product from Iceland 1975 - 1995¹⁴⁰

These changes, that is an increase in export, changes in the markets and increased competition in export also meant that the IFPC and SÍS lost their share of the export of frozen fish to other companies. Dr. Arnar Bjarnason found out in his Ph.D. study that IFPC had a 25% lower relative share of export of frozen fish product from Iceland in 1990/91 than in 1982/83, and the corresponding figure for SÍS/IS was around 16%.

Another significant change during this period was a increased freedom in exporting. First, the duopoly in export to the US was abolished in 1987. These changes came at a time when the US market had lost it place as the most important market for frozen fish to EEC markets. Therefore the changes did not affect the IFPC and IS as could have happened one or two decades earlier. In salted demersal species UIFP had had protection until 1st of January 1993 when the export of salted fish was de-monopolised. Since then UIFP has lost considerable share of the export of salted demersal species, going from almost 100% share to 51% share of the total volume of exported salted demersal species in 1996¹⁴¹. The rest of the export has gone to smaller companies, but around 5-6 companies export salted demersal fish in some considerable volume. Freedom has also been increased in the export of salted herring, where companies other than IHB have started to export it.

Although freedom has been increased, the government still puts pressure on companies in the industry to avoid internal competition and avoid too much

¹⁴⁰ Útvegur 1995.

¹⁴¹ SÍF Annual report 1996.

supply of fish on foreign markets. To do this, government and interest groups in the fish industry have formed a committee to control exports, where companies have to apply for permission to put their fish to auction markets. A successful recent judgement in a case where a company sued the government for putting barriers on its export of fresh fish to auction markets could change this control in the future¹⁴².

All the marketing companies that were Co-operatives changed their ownership form to limited liability, first with the establishment of Íslenskum Sjúvarafurðum (Icelandic Seafood), abbreviated IS, that took over the business of the fish function of SÍS in 1987. The next one to change was UIFP in 1992, then IFPC in 1996, and finally IHB changed its ownership into a limited liability company in the ownership of producers of salted herring in 1998¹⁴³. Following increased competition in exporting fish from Iceland and a declining catch in the late 1980s and 1990s, the marketing companies, mainly IFPC, IS and UIFP, have all changed their strategy and are increasingly starting to sell products for companies outside Iceland, both to utilise their marketing network and to maintain growth and profitability. This is in some part in coherent with the increased investment of Icelandic companies in the fish industry of foreign countries. The PMCs have also increasingly made contracts with other foreign companies not owned by Icelandic companies to take care of their marketing activities.

The export sector has changed quite a lot in the last decade, with increased freedom and entry of many small companies into the exporting sector. The main changes are associated with the change of the PMCs' strategy, that is, changes from selling only Icelandic fish to more international fish marketing companies. Another significant change is an increased emphasis of the PMCs on guaranteeing access to raw materials by buying shares in Primary processing companies (abbreviated PPCs). This applies mainly to IS which had shares in 12 - 15 PPCs in Iceland as well in foreign companies. Due to problems within IS and lack of profit, IS sold its share in the producers in 1999. UIFP has increasingly been investing in producers

¹⁴² Morgunblaðið, Samherji versus ríkið 1997.

¹⁴³ Morgunblaðið 22.07.98.

and sale companies of salted fish, both in Norway and Canada, but has not invested in PPCs in Iceland. IFPC has also invested in foreign production companies but in a very few cases bought shares in PPCs in Iceland. As well as IS, IFPC sold its share in the production companies in 1999.

The years 1997 –1999 have been big changes in the export sector in the Icelandic fish industry. The Icelandic Herring board was changed into Íslandssíld hf., in July 1998 and merged with UIFP on 1st of January 1999. IS faced troubles in their operation due to huge investment in secondary processing plants in US, France and in their new headquarters in Reykjavík. They also face operational problems with a project they were operating in Russia, where they lost a contract which they had invested quite a lot in. The problem of IS ended in 1999 when they merged with UIFP, making UIFP the biggest marketing company for fish in Iceland. In a similar way IFPC made less profit in 1998 and 1999, forcing them into changes in their operation, mainly by focusing more on their core activity, that is the sale of frozen fish. Hence, IFPC has gone out of related businesses such as transportation, and sold its share in other companies. In the end of 1999 only two of the four Primary Marketing Companies are in operation. UIFP has increased its operation quite a lot in size and diversified its operation from only being a marketing company for salted fish into being an international marketing company focussing on chilled and frozen fish. On the other hand IFPC has focused its operation as being an international marketing company for frozen fish.

IV.2.6.3 Market developments

As can be seen from previous chapter the markets for the Icelandic fish products have changed quite a lot over the past two decades. The European market has become the most important market and the Japanese market has increased its share considerably. The long term traditional markets like the US and former Soviet Union have declined for the past decade. It is not just the changes in markets areas that affect the fish industry but also changes within the markets. The main developments in Europe and the US are the increased market share of supermarkets. An example of this growing role is

the high share of the big four supermarkets in the UK where Tesco, Sainsbury's, Asda and Safeway account for about 45 percent of the total UK grocery sales¹⁴⁴. Thereof Tesco has around 16 percent of the total grocery sales. In addition, there is a growing interest on the UK markets in own-label products that account for around 45 percent of the total supermarket sales in the UK¹⁴⁵. This emphasis on own-label goods is however, not as high in other European markets, for example in France¹⁴⁶. This consolidation that can be seen in the UK has also been noted in the US where consolidation has increased significantly since 1995¹⁴⁷. In the US, the consolidation has been highest within the four biggest supermarkets, their share having risen in 1998 from 9 percent to 29 percent of total grocery sales in the US¹⁴⁸.

It has been pointed out that the increased power of the supermarkets and increased competition between supply chains (value chains) creates more pressure on supermarkets to improve the relationships within the supply chain to make it more competitive and effective. Dedman and Fearne phrase this as the "Paradox of Power" where with the increased power of the supermarkets, emphasising on own-label products, they are getting increasingly dependent on fewer and larger suppliers¹⁴⁹. Hence, supermarkets must concentrate more on cooperation with suppliers for long-term partnerships in mind¹⁵⁰. In the same way it has been pointed out that it is getting more difficult for go-it-alone strategy and small companies to be competitive in the market¹⁵¹. It is clear that developments on the food markets, e.g. increased concentration, will affect the structure of the Icelandic fish industry. It depends on how deep into the markets producers are selling, but this development indicates a stronger need to join a

¹⁴⁴ Fearne, A. & Dedman, S.

¹⁴⁵ Fearne, A. & Dedman, S.

¹⁴⁶ Based on interviews with managers of ICFP and UIFP

¹⁴⁷ Kaufman, R. P.

¹⁴⁸ Kaufman, R. P.

¹⁴⁹ Fearne, A. & Dedman, S.

¹⁵⁰ Cook, R.; Fearne, A. & Dedman, S.; Wysocki, F. A.

¹⁵¹ Wysocki, F. A.

competitive supply chain rather than pursue a go-it-alone strategy (see discussion in chapter V in relation to a Literature Review for more discussion about the supply/value chain and go-it-alone strategy).

Consolidation in the retailer section can easily affect the Icelandic fish industry. It varies from one market to another, however, how far into the markets the companies are selling their fish products. In the UK markets for example the products of the secondary processing plants of ICFP are aimed at the supermarkets. This status of the supermarkets and their strategy of own-label makes it difficult for other producers to pursue their own label strategies. These changes also affect the producers in such a way, that it could be difficult for small producers to gain direct access to the supermarkets with their products. Rather, they would need to sell to some intermediate that would then have access to the supermarkets. On the other hand, in most cases, the Icelandic fish products are not marketed directly to supermarkets, but rather into secondary processing, to restaurants or to other companies that distribute or sell the products deeper into the markets. This, for example, is the case on the Japanese market where the products from Iceland are more or less industrial products for further processing or go on to an auction market. The same can be said of the salted fish that is mainly sold to the Mediterranean area which is very much a traditional market with small shops and distribution companies selling into these small shops.

IV.2.7 Profitability and Development of Companies

As can be seen from table IV.6 the profitability of the fishing industry has varied quite a lot since 1980. From 1980 to 1994 the fishing industry has only returned profit in two years, 1986 and 1990. The processing sector has been little better and returned profit in 8 years out of 15. Due to the vertical integration of the processing into the fishing sector and vice versa it is rather unrealistic to look just on the sectors separately. It is more realistic to look at the results from the industry as a whole. As can be seen from table IV.6 the over-all profitability has been rather bad; the industry has returned profit for 6 of 14 years. The profit has varied from 0.7% as a percentage of revenues in 1987 to 4.9% in 1990.

Year	Fishing and Processing	Fishing	Processing	Freezing	Salting and Drying	Marketing:	
						IFPC ¹⁵²	UIFP ¹⁵³
1980	4.0	-3.9	8.3	2.3	18.2	N/A	N/A
1981	4.0	-1.0	6.6	1.3	13.7	N/A	N/A
1982	-9.4	-39.9	5.8	4.4	7.2	N/A	N/A
1983	-4.4	-13.0	0.5	0.5	4.1	N/A	N/A
1984	-8.0	-18.9	-1.4	-1.4	-5.0	N/A	N/A
1985	-2.4	-1.8	-2.8	-4.6	-1.8	0.93	1,4
1986	4.7	6.2	3.7	4.1	7.6	0.63	1,9
1987	0.7	0.0	1.3	0.0	5.5	-0.18	3,7
1988	-8.5	-7.7	-9.2	-14.1	-5.2	-1.65	2,4
1989	-3.6	-4.4	-3.0	-1.1	-4.9	0.4	2,1
1990	4.9	7.7	2.1	4.8	1.5	1.74	4,4
1991	-2.7	-2.2	-3.1	-1.7	-2,7	0,98	1,3
1992	-3,5	-6,6	-0,7	-0,1	-0,9	1,9	-1,4
1993	-5,1	-11,9	1,1	1,2	-3,0	2,73	1,8
1994	1,9	-2,3	5,3	8,6	-0,6	2,66	3,6
1995	3,0	4,2	1,9	2,1	-0,9	1,23	1,8
1996	0.8	2.7	-0.9	-4.3	-4.0	2.73	1.1

Table IV.6 Profit from regular operation as a percentage of revenues 1980-1996¹⁵⁴

During the period 1985-1996 IFPC returned profit all the years except 1987 and 1988. UIFP returned profit for all the years except for 1992 the last year before the ownership change. Hence, comparing the fishing and processing sector to the marketing companies it is clear that the profitability of the marketing companies has been far better than the processing sector. It has to be considered that the marketing companies were operated as non profit companies, UIFP until 1993 and IFPC in 1997. Due to this the marketing companies returned the profit to their producers in the end of the year after they had paid their costs and investment that year.

Another aspect of the profitability and financial status of the companies in the fish industry is the equity that the companies have built up. The equity ratio in 1988 was 5.3% for the whole industry. In 1990 this ratio was 15% and in 1996 it was up to 26%¹⁵⁵. This is of course a mean figure for the whole industry, so there are companies with higher equity ratio and

¹⁵² Figures for the period before 1985 were not available by IFPC.

¹⁵³ Before 1985 UIFP used different methods of presenting their financial statement making access to these figures difficult.

¹⁵⁴ Þjóðhagsstofnun, Atvinnuvegaskýrsla 1994; Sögulegt Yfirlit Hagtalna 1945–1995; UIFP Annual reports; IFPC Annual Reports.

¹⁵⁵ Runólfsson, Þ.B.

companies with lower ratio. This development of the equity of companies in the fish industry demonstrates very well the changes over the last decade, where increased freedom in the economical environment and more established financial markets have brought in new demands on the companies in the industry to return profit and return dividends to the owners. This is a big change from what was known before, mainly due to hand controlled economy, where the government controlled the rate of exchange of the Icelandic króna in accordance to some zero profit policy where the aim was to keep the profit of the fish industry at zero. In this environment profit was almost a bad thing in the view of the politicians.

The main characteristic of this development over the last decade is concentration where companies have merged and become bigger. This is relevant for companies in all the sectors of the fish industry, that is, in fishing, processing and exporting. To see this concentration it is helpful to look at the share of the ten biggest companies in the assigned quota of each year. In the fishing year 1995/96 the ten biggest companies had a 26.51% share of the total quota, but in 1998/99 the same figure was 32.22%¹⁵⁶ (see table IV.7). It is interesting that all these ten companies are both in fishing and processing, that is, vertically integrated companies. Also, just one of the ten biggest is not in the business of the Principle marketing companies, that is, Samherji hf., which more or less takes care of its own marketing matters.

	1998/99	1997/98	1996/97	1995/96
Samherji hf	5.56%	5.04%(1)	4.51%(1)	3.78%(3)
Haraldur Böðvarsson hf	4.61%	4.28%(2)	3.42%(4)	2.62%(4)
Útgerðafélag Akureyrar hf	3.90%	3.41%(4)	3.72%(3)	3.91%(2)
Þormóður Rammi – Sæberg hf	3.87%	4.23%(3)	1.49%(12)	1.66%(11)
Grandi hf	3.17%	3.16%(5)	3.80%(2)	4.43%(1)
Síldarvinnslan hf	2.53%	2.24%(8)	2.56%(5)	2.36%(5)
Fiskiðjan Skagfirðingur hf	2.27%	2.16%(9)	2.28%(6)	2.04%(7)
Þorbjörn hf	2.26%	2.31%(7)	0.97%(18)	1.17%(16)
Íhúsfélag Vestmanneyja hf	2.14%	1.76%(14)	2.19%(7)	1.90%(8)
Hraðfrystihús Eskifjarðar hf	1.91%	1.82%(13)	1.74%(9)	1.38%(14)
Total share of the ten Companies	32.22%	30.41%	26.68%	25.25%
Ten biggest each year	32.22%	31.24%	27.82%	26.51%

Table IV.7 Quota of the ten biggest companies as a percentage of assigned quotas each year¹⁵⁷

¹⁵⁶ Runólfsson, Þ.B.

¹⁵⁷ Runólfsson, Þ. B., page 77. The order of the companies is in the parenthesis

Most of the changes in the order of the companies seen in table IV.7 can be traced to mergers between companies in the fish industry and therefore the companies have added to their quota. There is no sign that this development will not carry on, as evidenced, for example, in 1999 when Íshúsfélag Vestmanneyja hf planed to merge with three other companies in the fish industry. More examples could be taken but they all point towards more concentration in the fish industry over the coming years.

IV.3 Conclusions

The Icelandic fish industry has gone through great changes over the last 20 years. These changes reflect the economical and political environment in Iceland during this time. The main characteristics of these changes are concentration, where the companies are getting bigger and fewer. The industry is getting more stable where the profitability is getting better, especially over the last five years. Bigger companies mean that companies have increased their ability to take on more complicated issues than just producing raw material. This is reflected in increased emphasis on issues such as the development of new products and marketing matters. From this discussion about the Icelandic fish industry four factors can be pointed out as main factors that have influenced the development of the industry for the last 10-15 years. These issues are the implementation of the quota system, increased freedom in the export of fish from Iceland, increased economical freedom in Iceland and finally the increased entrance of companies in the fish industry to the public stock market.

The first factor, the implementation of the quota system, was first introduced in 1983 and later on all species in 1990. Due to the quota system better control has been gained of the fishing stock, which has lead to higher quotas on species such as cod. The quota system has also made planning better for the companies- they know better what they have and how they can do their planning in accordance with that. The quota system has also created pressure for concentration in the fishing sector, where decreased quotas in the beginning meant that boats and trawlers faced operational difficulties due to low utility of the investment. In studying the

concentration it is interesting to see that the decline in the fishing fleet has been dramatic from 1992 after a rather slow decline since the quota system was introduced in 1984¹⁵⁸. It is suggested here that this can be traced to the law that allowed the ITQ and the high quota price that followed. This has made the option of leaving the industry with a profit attractive for the owners of companies that have been facing operating difficulties and therefore supported a more profitable industry. Hence, it is argued that the ITQ is one of the preconditions for making this concentration possible by allowing owners of fishing vessels to sell their quotas and leave the industry without losing money on the investment in vessels. Due to high vertical integration of fishing and processing this concentration is also the case in the processing sector, where decreasing quantities of fish for production have forced producers out of business, especially those who are not operating their own boats or trawlers. In the same way, as the high degree of vertical integration has enabled this concentration in the processing sector, it is claimed that this vertical integration is one of the prime reasons for the ITQs to be effective in the industry, avoiding the negative effect of the quota system. These proposed negative effects are for example the lack of power balance between the two sectors, leaving the power in the hands of the quota holders. Hence, the vertical integration has maintained a certain power balance in the industry preventing the fishing sector from becoming too powerful.

An other factor supporting this concentration is the entrance of companies in the fish industry to the stock markets has increased their accessibility to capital, where companies have been able to get capital to buy out smaller companies that often have been facing operational problems. The entrance of the fish companies to the stock markets have also put pressure on the management to return profit to increase the value of their shares. This development is in accordance with increased freedom in the Icelandic economy where the freedom has given companies access to capital both in Iceland and abroad. This freedom enables companies to transfer capital between countries and invest in other countries, which has been the case for

¹⁵⁸ Runólfsson, B. & Árnason, R., 1996.

the Icelandic fish industry. This freedom is in some cases not the same in both directions, where foreign companies have limited access of investment in the Icelandic fish industry. The last factor in influencing the development of the industry is increased freedom in exporting fish from Iceland. This freedom was not gained until 1993 when export of salted fish was demonopolised. This has meant that the traditional primary marketing companies have faced increased competition both from other marketing companies and also from some producers who have been selling the products on their own. The increased power of supermarkets discussed earlier in this chapter can in many ways work against this development of individual companies attempting to sell their own products unless they want to sell to intermediaries in the value chain.

All this has meant that the Icelandic fish industry has had to rely much more on its own ability and development to be able to return profit, rather than putting pressure on the government for deflation or other governmental interference to guarantee the operational basis of the companies. This has created a much healthier business environment for the companies in the fish industry. Despite the positive affects of this development there are negative affects as well, especially for the small villages along the coast where bigger companies have bought the quota. This transferability of quotas has been criticised. The criticism is mainly that in some cases the quota is sold, or whole companies are sold, away from the village leaving the inhabitants without employment. In the same way the value attached to quotas has been criticised where the owners of fishing vessels and boats are granted a quota with paying minimal price for it, which they can then sell for a high price. This has in some cases been a motivation for boat owners to sell their boats and quotas where they get most of the price for the quota, not the boat. Despite this criticism, it is clear that the fish industry is operating in a much healthier business environment than it did 10 years ago, where increased freedom is the key factor today. This has caused great changes which are in many cases just the beginning, and all indications point to more concentration, where the production companies will increase their value

creation through product development instead of selling raw material for further production abroad.

V Literature Review

Strategic alliance is a very wide concept that is increasingly used to cover almost all aspects of companies' cooperation. The literature on strategic alliances is young and gets its basis from heterogeneous sources of cooperation of companies. Literature and research on the phenomena of companies' cooperation has taken many forms and names. One reason for this is that the literature encompasses organisational marketing often called "*business to business marketing*". Axelsson claims that literature on business-to-business marketing and organisational buying behaviour has developed into two quite different traditions¹. The first, and original approach is mainly connected with academic research and writers in the United States and their writings about buyers or sellers, which are generally led from consumer marketing. The second approach is traced to Europe where the work has been much more influenced by organisational theories and more focused on the "space" between organisations and the network of relationships between companies that are involved². In addition to these two perspectives it is necessary to include the long Japanese tradition for companies' networks and close cooperation between companies and their suppliers.

This chapter starts with a general discussion about the definition of strategic alliances, their types and characteristics. In the second part the discussion moves on to study the rationalisation of strategic alliances from the economic and organisational point of view where the main emphasis is on vertical alliances and relationship in the value chain. The third part of this literature review will then study the newly emerging network perspectives that are increasingly quoted in discussion about companies' relationships. The fourth part will study the governance of strategic alliances; the main emphasis will be on governance of strategic alliances in the value chain and on what influences the governance.

¹ Easaton, G.

² Easaton, G.

V.1 Definitions of Strategic Alliances

The definition of a strategic alliance is often unclear but in a broad sense it involves cooperation between two or more companies³. This definition can be used to cover almost all relationships that companies are involved in. An example can be taken from Badaracco where, in his book “Knowledge Link”, he uses the term strategic alliances to describe all types of cooperating relationships between companies and competitors, customers, suppliers, governments bodies, universities and labour organisations⁴. Other explanations are more specific. For example, James Jr. and Weiderbaum, in their book “Strategic Alliances”, suggest that companies “*share some risk in the investment they have made, financially or otherwise, in the common activity*”⁵. There, the authors exclude such a long-term commitment as suppliers’/customers’ relationships. It can be argued that the increasingly common form of suppliers’/customers’ relationship (as will be discussed in chapter V.2.1 of this thesis), called a “comaker,” is a strategic alliance because the suppliers in this case often take on a risk in development of products⁶ with their customers. In a “comaker” alliance, the shared risk and benefits are undoubtable and the cooperating arrangement is often so close that, in some cases, the boundaries between companies are getting blurred⁷. Contract and Lorange have forwarded a definition of strategic alliances, which is based on the degree of interdependency of companies involved in the strategic alliances⁸. This definition covers the field from the extreme of a complete merger, on the one hand, to informal arrangements on the other hand. Several types of strategic alliances lie along this continuum. Figure V.1 shows how independent the companies in the alliances are to each other, in this respect.

³ Lorange, P. & Roos, J., 1993.

⁴ Badaracco, J. L. Jr.

⁵ James, Jr. & Weiderbaum, M., page 11.

⁶ Product is in this essay used over both hard product as well as service that companies provides.

⁷ Mariotti, L. J.; Badaracco, J. L. Jr.

⁸ Contractor, J. F. & Lorange, P.

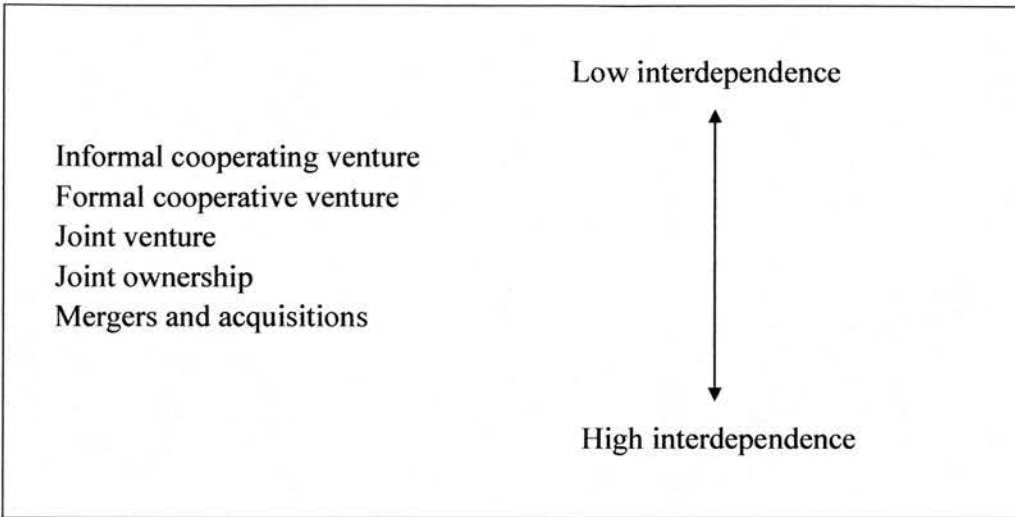


Figure V.1 Strategic alliances' options between the parent firms⁹.

According to Contractor and Lorange, strategic alliances could include any of the categories along this continuum, from informal cooperating arrangements to mergers and acquisitions. Harrigan (1988) put forward the definition that “*strategic alliances, joint ventures, cooperating agreements and so forth are partnerships among firms that work together to attain some strategic objective*”¹⁰. Hence Harrigan is taking strategic alliances as one form of the relationships between firms. In the literature today it is reported that the term “strategic alliances” is increasingly used to cover all types of cooperating activities between companies¹¹. On the other hand, the Centre for the Study of American Business, Washington University, has categorised strategic alliances and their alternatives for global marketing, where strategic alliances are split up into two groups with and without equity share (see Table V.1).

⁹ Lorange, P. & Roos, J., page 4.

¹⁰ Harrigan, R. K., page 205, 1988.

¹¹ Contractor, J. F. & Lorange, P.; Lorange, P. & Roos, J.; Badaracco, J. L. Jr.

Alternative Business Responses to the Global Marketplace	
Alternatives	Forms
Direct strategies for marketing abroad	Exporting Turnkey operations
Cooperating contractual agreements	Licensing Franchising Subcontracting
Wholly owned affiliates	Greenfield operations Mergers and acquisitions
Strategic nonequity alliances	R&D cooperatives Technology swaps Joint production/ marketing agreements
Strategic equity alliances	Joint ventures Joint equity swaps Affiliates Other investment alliances

Table V.1 Alternative Business Responses to the Global Marketplace¹²

If the definition proposed by the Centre for the Study of American Business, shown in Table V.1 is compared to prescribed definitions of strategic alliances in this chapter, it is obvious that it is much narrower. Some authors exclude licensing, franchising and subcontracting as a form of cooperating contractual agreement whereas other authors have included them. It can be argued that cooperating contractual agreements are, in almost all cases, very close business relationships between companies where the partners are aiming at the same strategic objectives. Hence, in conclusion, a broad definition of strategic alliances can be used to cover the whole range of cooperative relationships between companies, which are aiming at the same strategic objectives. The definition that will be used in this dissertation is that strategic alliances are where *two or more companies cooperate together to attain shared strategic objectives*. The definition includes the idea that a company is in a close strategic alliance with its suppliers and customers.

¹² James, S. J. Jr. & Weidenbaum, M., page, 104 - 105.

V.1.1 Types of Strategic Alliances

The most common type of strategic alliance is presumably the form of suppliers’ and customers’ relationships. As will be described in more detail in Chapter IV.2, the new suppliers’/customers’ relationships, that are built on a “co-makers” principle, require long term business relationships and close cooperating arrangements between companies. Other forms of strategic alliances are becoming increasingly popular and used in business today, both in cooperation between companies in two or more countries and in the domestic market as well¹³.

Lorange and Roos split strategic alliances into four archetypes according to the nature of the “parents”¹⁴ input of resources and their retrieval of output from the strategic alliances¹⁵. As can be seen from Figure V.2 these archetypes are ad hoc pool, consortium, project-based joint venture and full-blown joint venture.

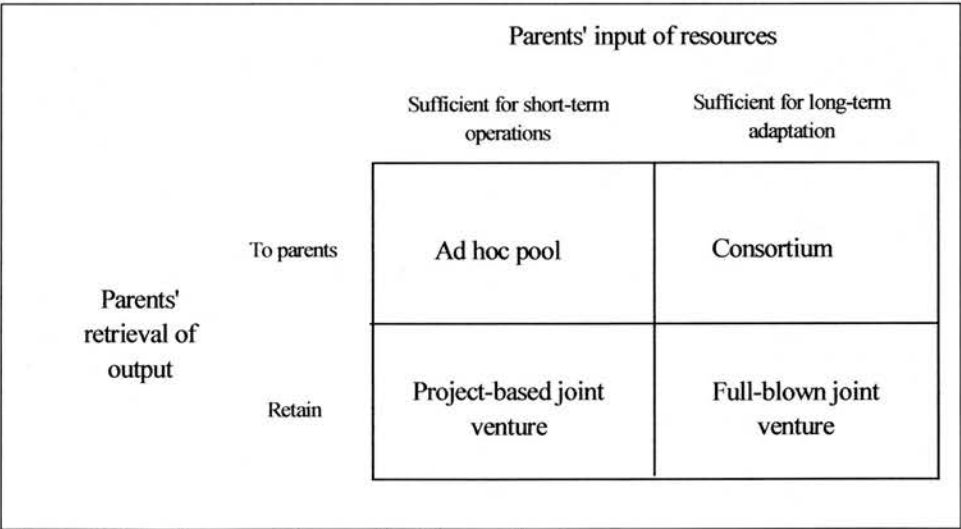


Figure V.2 Archetypes of strategic alliances¹⁶

The *ad hoc pool* attempts to meet the need for short-term alliances, which do not demand many resources from the “parents”. Examples of *ad-hoc* alliances include joint R&D programmes where, for some short time,

¹³ James, S. J. Jr. & Weidenbaum, M.
¹⁴ In this dissertation the word “parent” covers the companies that form the strategic alliances and the word “child” is used for the joint venture company that is formed.
¹⁵ Lorange, P. & Roos, J.
¹⁶ Lorange, P. & Roos, J., page 10.

companies decide to join forces to develop new technology or products; after their development, the resources will go back to the companies¹⁷. The *consortium* type, on the other hand, demands more resources from the “parents” but the value creation in the strategic alliances is given back to their “parents”. Consortium types of alliances can be found in “*more involved consortium research programmes among several parties, each having too small a resource base to carry out all the research on its own*”¹⁸. The third archetype is the *project-based joint venture* where the “parents” form a joint venture to cover some project-based activities and demand a minimum strategic resource from the “parents”. The last form of archetype is the *full-blown joint venture*, which often makes the strategic alliances themselves more independent from their “parents” and their resources than the other archetypes.

These archetypes of strategic alliances are helpful in studying the nature of the alliances and the motivation for going into such arrangements. However, it is important to recognise that the nature and motivation for the strategic alliances can change over the course of the alliances. For example, strategic alliances that start out as project-based joint ventures to cover some short-term activities can be developed over time into a full-blown joint venture. Although this category is helpful there are many forms of strategic alliances that can be categorised into one or more of the alliances’ archetypes. To get a better view of the forms of strategic alliances, it is helpful to categorise them in a way similar to that in Table V.1 and Figure V.1. In Table V.2, strategic alliances are categorised into three main types: joint venture; collaborative venture and other types of alliances. Two other groups are also mentioned, i.e. informal business relationship and mergers and acquisitions. Both these types border on being called strategic alliances but are included here because it is necessary to recognise that these forms of relationships can be the first and the last steps respectively, in alliance formation.

¹⁷ Lorange, P. & Roos, J.

¹⁸ Lorange, P. & Roos, J., page 46.

Strategic Alliances		
Types	Example	Characteristics
<i>Informal Business Relationship</i>	<i>Membership in same professional organisation. Friendship</i>	<i>Problem discussion groups between managers of companies which is often the first step in formal alliances between companies</i>
Joint Venture	Form a separate company to take care of the joint activity.	Shared equity and management responsibility.
Collaborative Venture	Shared projects.	Common form in industry that demands high R&D cost or industry that is risky, for example oil industry. Usually no equity share.
Other types of Alliances	Licensing. Franchising. Subcontracting. Close relationship with suppliers' and customers'.	Do not need equity share, though in some cases it follows close business relationships between companies.
<i>Merges and Acquisitions</i>	<i>Companies merge into each other or are acquisitions from other companies.</i>	<i>Possible the last phase in strategic alliances between companies</i>

Table V.2 Category of strategic alliances¹⁹.

V.1.2 Characteristics of Strategic Alliances

To get a better view of strategic alliances it is helpful to look vertically and horizontally at the companies that are in such alliances²⁰. In vertical alliances (often called x-type) the companies form strategic alliances with companies in the value chain, for example, in producing raw material for their own use or to market their products at home and/or in foreign markets. Typical vertical alliances can be in the form of a close business relationship between companies and their suppliers and customers, such as co-producers subcontracting, or in a form of a joint venture that is either behind or ahead in the value chain. In vertical alliances the main object, in most cases, is to add more value in the process and to get better access to factors like raw material, technology, distribution, services or markets. These vertical alliances can also be established in order to gain access to knowledge, for example, for manufacturing companies to go into alliances with marketing companies.

¹⁹ This table is the authors presentation.

Horizontal strategic alliances, on the other hand, may be between companies in a similar field as in the cases of the Icelandic fish industry presented in chapter IV. In many cases they are in joint research and development (R&D) programmes or joint production agreements with other companies in order to broaden their production scope. Joint R&D programmes are common in highly technical industries and in aerospace where the R&D costs and risks are high. Horizontal alliances such as joint R&D programmes are likely, for that reason, to be more knowledge-based than vertical alliances. The aim is to gain access to knowledge and technology that one company would not possess using only its own resources.

Many types of strategic alliances can be in both the vertical and horizontal form. These types can range from an informal relationship between companies without equity share, to the establishment of equity-shared companies.

Another way to look at strategic alliances is to examine them in terms of the relationship or links between the companies. Badaracco splits these links into two main types: product links and knowledge links²¹. He then splits knowledge links into two further categories: “migrating knowledge” and “embedded knowledge”. “Migrating knowledge” can move easily from one company to another, for example in the form of blueprints or a set of business systems, in alliances such as franchising and licensing. “Embedded knowledge” is knowledge that lies in a *“specialised relationship among individuals and groups and in the particular norms, attitudes, information flows, and ways of making decisions that shape their dealings with each other”*²². Knowledge and the ability to learn are crucial factors for companies’ success in the long run in the modern environment. In this regard “embedded knowledge” is especially important because it is not as easy to buy as “migrating knowledge”.

The purpose of product links is, in most cases, to fill gaps in product lines, often with a product from companies in low-cost countries, which the

²⁰ James, S. J. Jr. & Weidenbaum, M.

²¹ Badaracco, J. L. Jr.

²² Badaracco, J. L. Jr., page 79.

companies are not able to produce themselves²³. This form of alliance is well known in the automobile industry where the US companies made alliances with Japanese and other Asian companies in order to produce small cars, which US firms had not produced previously. Product links between companies are usually in the form of joint ventures, long-term suppliers'/customers' relationships or subcontracting often with minority equity share²⁴. Companies can benefit from product links in many ways but the most obvious are, cost and risk reductions, flexibility and broader product scope. Companies, especially from the US and W. Europe have been criticised for moving their manufacturing too quickly to low cost areas or for making alliances with companies there. This has led to instances where companies have not tried to increase their competitiveness within their domestic market but have used the opportunity to move the production to low cost areas as an escape from the problems they are facing at home²⁵.²⁶ Although the main purpose of product links is to fill product gaps, it is possible that some knowledge will move with the product. Initially this knowledge is more likely to be "migrating knowledge" but in the long run will probably start to add to the "embedded knowledge" of the local partner companies.

In knowledge links, the main objective in the alliances is to create and learn new knowledge²⁷. Typical knowledge links occur when a company forms an alliance with other companies in R&D activities or with universities or other research institutions. It is not unusual for one company to form a multitude of knowledge links with other companies, universities, and other organisations in order to add new knowledge to their own organisations. Knowledge links can be formed to get both "migrating" or "embedded" knowledge but it is more likely that companies are trying to increase their "embedded" knowledge to look for ways to differentiate themselves from their competitors, for example by innovation.

²³ Badaracco, J. L. Jr.

²⁴ Badaracco, J. L. Jr.

²⁵ Hayes, H. R. & Pisano, P.G.

²⁶ Hayes, H. R., Wheelwright, C. S. & Clark, K. B.

²⁷ Badaracco, J. L. Jr.

Hayden Shaugnessy pointed out that the emphasis on collaboration between companies has moved from formal and product links towards more informal alliances where the emphasis is much more on knowledge, as for example joint R&D as well as joint venture in penetrating new markets (see Table V.3 showing Hayden Shaugnessy's summation of changes in companies' collaboration)²⁸.

Development of Collaboration	
Traditional inter-firm collaboration	New alliances
Merger	Loose alliances based on new corporate forms such as the European Economic Interest Group
Acquisition in new sectors for diversification	Corporate networks
Local partner acquisition to penetrate new geographical markets	Joint product development
Joint ventures to create new production capacity	Joint ventures to penetrate new markets
Patent and other forms of licensing	Short-term partnerships for contract acquisition
Franchises	Partnerships under public sector contracts
Product sharing and reciprocal marketing rights	Inter-company collaboration by objectives
Cross-shareholding	Collaborative research and development (R&D)
Diversification through portfolio management	

Table V.3 Development of collaboration of companies²⁹

Furthermore Axelsson claims that “*formal cooperation seems to be a minor part of the totality of inter-corporate cooperation. The fundamental possibilities for cooperation lie in everyday informal activities within continuing business relationship*”³⁰. This development seems to be suggesting that alliances are becoming more informal, knowledge based, objective and market driven than they were in the past³¹. Hence it is important to recognise that strategic alliances can develop from ad-hoc alliances or informal relationships to full-blown joint ventures and even to merging of the partners. Therefore, it is important that managers and others who are involved in the strategic alliances have a good understanding of both the nature and characteristics of the alliances as well as the objectives

²⁸ Shaugnessy, H., page 11.

²⁹ Shaugnessy, H., page 11.

³⁰ Axelsson, B., page 198.

³¹ Devanna, A.M. & Thichy, N.

of all partners in the alliances. This understanding can help companies and managers to identify alliances that are suitable for the company to join and also what resources need to be put into the alliances, both from the viewpoint of their own company and other participants. An understanding of the alliances and objectives of the participants in these alliances is also essential to*8 ensure that they are manageable in the future and have the opportunity to develop.

V.2 Rationalisation of Strategic Alliances

The aim of this section is to make an attempt to answer the basic question of how strategic alliances can be rationalised. It has been pointed out that in order to establish strategic alliances and to then maintain them, they need to be more effective and efficient than their alternatives³². Jarillo claims that the basic condition behind the effectiveness of alliances is that the external cost of the transaction is higher than the cost would be if the transaction were carried out inside the alliances (internal cost). Furthermore he claims that another basic condition behind effectiveness is that in the long term the profit of the alliance is seen to be superior to the profit that can be obtained by going it alone or by establishing short-term relationships with other companies³³.

When studying the rationalisation behind strategic alliances it is helpful to start looking at economic theories about business-to-business marketing or suppliers' and customers' relationships. These theories have been called transaction theories and can be traced originally to R.H. Coases (1937) and more recently Williamson (1975). They aim to explain that the economic system is coordinated by factors other than pure price mechanisms of the free market³⁴. The essence of Williamson transaction cost theory is that on the one end is the hierarchy, which is a fully vertical integrated firm, and on the other end is the free market where the price of the transaction is the ruling force. This means that if the transaction cost is lower in the free

³² Jarillo, C. J.

³³ Jarillo, C. J.

³⁴ Larson, S.

market, where companies can buy their subcomponents rather than making themselves, then the market will be used; then in the same way, if and when the company can make the subcomponents itself it will integrate the production in its own company³⁵. Hence, it is given that there are only two stable forms of organising the relationship between suppliers and buyers, that is the free market and the vertical integrated firm. Strategic alliances have then been located between these two poles and categorised according to the degree of vertical integration, as Lorange and Roos do (see Figure V.3.).

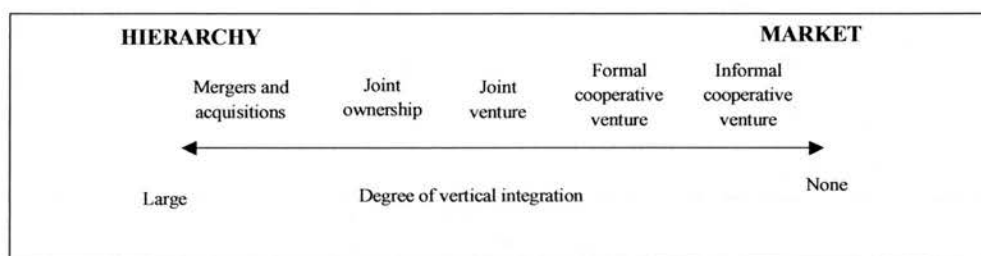


Figure V.3 Strategic alliances' options in terms of degree of vertical integration³⁶

The idea that strategic alliances should be viewed as an intermediate between the free market and hierarchy has been increasingly criticised³⁷. It has been pointed out that viewing the strategic alliances this way dismisses the third dimension of coordination, and cooperation that can lower the transaction cost and make companies quicker to respond to changes and more flexible than in the case of hierarchy or the market³⁸. Ouchi approached this problem of using the two dimension scale by splitting hierarchy into two parts, the “bureaucracy” which reflects the traditional hierarchy and the “clan” which describes long term relationships, carried out through non-specific contracts within the formal environment of an organisation³⁹. In the same way the market is split into two parts the “classic market” where the relationship is built on a spot basis, and another part which Jarillo calls “strategic network”⁴⁰. These could equally be called

³⁵ Jarillo, C. J.

³⁶ Lorange, P. & Roos, J., page 3.

³⁷ Axelsson, B.; Larson, S.; Jarillo, C. J.; Easton, G.; Osborn, N. R. & Hagedoorn, J.

³⁸ Jarillo, C. J.

³⁹ Jarillo, C. J.

⁴⁰ Jarillo, C. J.

strategic alliances where the relationship is built on much closer cooperation with suppliers⁴¹ (see figure V.4).

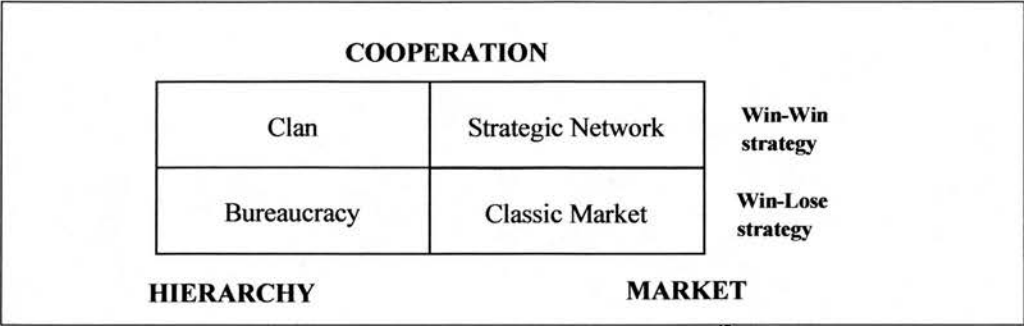


Figure V.4 The four modes of organising economic activities⁴²

In accordance with this, Ouchi has put in a new dimension into the discussion about companies’ relationships built on “fairness” or win-win (cooperative) relationships instead of the “opportunism” of Williamson’s transaction cost theories, which build on win-lose (competitive) relationships between suppliers and customers⁴³. Hence, the economy of the strategic alliances is not just built on lowering the transaction cost but rather on increasing the value in the relationship by working together in the value chain to improve the value adding process by synergising their activities and resources. Larson maintains that the strategic trend has moved from the “transactional perspective”, where the transactional cost decides the form of the relationship, towards an “interaction approach” with various kinds of socio-economic alliances⁴⁴. In order to study this closer and move the focus of this literature review closer to the essence of the following empirical research, it is helpful to study the value chain and its relationship in order to be able to analyse the strategic alliances.

V.2.1 Value Chain and Strategic Positions of Companies

Porter defines the role of the value chain as a template, which allows managers to examine in a systematic way all the activities a firm, performs and how they interact, which is necessary for analysing the source of

⁴¹ Jarillo, C. J.

⁴² This picture is the authors presentation but build on Jarillo, J. C., page 34.

⁴³ Jarillo, C. J.

⁴⁴ Larson, S.

competitive advantage⁴⁵. Porter put great emphasis on the strategic position of companies in what he calls the value system, which is the embedded value chain from suppliers to buyers. Furthermore he claims that strategy is about coping with competition and that companies' competitive strength depends on five major forces: threat of new entrants, threat of substitute products or service, bargaining power of suppliers, bargaining power of buyers and rivalry among existing competitors⁴⁶. In many cases this emphasis on companies' bargaining power over suppliers and buyers has led to a too narrow view of the whole value adding chain and put companies in win-lose competition with their suppliers and buyers. This view is reflected in the transactional perspective where the traditional view is that companies have a single value adding chain, whereby they build their relationship with suppliers and customers on one specific transaction where companies buy in products from suppliers, add value to it and sell it on to customers⁴⁷. Furthermore Pfeffer concludes in his review of strategic contribution that strategic research has been characterised by a fundamentally internal focus, with the single organisation as the unit of analysis⁴⁸. This is especially true in US companies where the suppliers have traditionally been made to compete against each other on price and kept away from information about customers' production to ensure that companies will not have to depend too much on their suppliers⁴⁹. The main emphasis in such a strategy is that the competitive strength of each company depends on obtaining the right position in the value chain whereby the company has to choose the right products, market segments and value-adding activities and to possess bargaining power over others in the chain. This view is increasingly criticised as being too narrow and isolated⁵⁰.

Normann and Ramírez argue that it is no longer enough just to add value to the product or have the right position in the value chain, rather that

⁴⁵ Porter, E. M., 1985.

⁴⁶ Porter, E. M., 1994.

⁴⁷ Larson, S.

⁴⁸ Axelsson, B. (based on Pfeffer, 1987).

⁴⁹ Helper, S.

⁵⁰ Axelsson, B.; Larson, S.; Jarillo, C. J.; Easton, G.; Osborn, N. R. & Hagedoorn, J.; Clegg, R. S.

companies have to *reinvent* the value creation in the value chain⁵¹. They go on to say that *"the focus of strategy analysis is not the company or even the industry but the value-creating system itself, within which different economic actors-suppliers, business partners, allies, customers - work together to co-produce value"*⁵². In this way the key strategy is to rethink the relationship that the firm has with other companies in order to be able to create value in new forms for customers. This approach is different from the traditional view which demands that managers understand well the whole process because much of the value creation occurs in the supplier and customer's chain⁵³. Larson takes a similar view of what he calls the *"interactive perspective"* and claims that it is necessary to focus on the *"overlapping links in activities function between buyer and seller"*⁵⁴. He continues by saying that the *"common work arena thus becomes the object of study instead of the individual company"*⁵⁵. Furthermore Porter pointed out the connection between the value chain and organisational structure and states that the organisational structure of companies is often incapable of providing coordinating mechanisms to optimise the linkages in the value chain⁵⁶. Hence, an understanding of the whole process and the interaction with other players therein is necessary to optimise the linkages within the value adding chain with the aim of increasing value creation, which may have the added benefit of lowering costs in longer run.

In order to explain this new view, Normann and Ramírez take an example from IKEA's system, which offers its customers a part in the value chain by giving them the option to assemble the furniture at home⁵⁷. Part of IKEA's programme is to create a long term relationship with its suppliers in which IKEA offers them high volume orders, technical assistance, leased equipment and advice on bringing production up to world quality standards.

⁵¹ Normann, R. & Ramírez, R.

⁵² Normann, R. & Ramírez, R., page, 65 - 66.

⁵³ Johnson, G. & Scholes, K.

⁵⁴ Larson, S., page 41.

⁵⁵ Larson, S., page 41.

⁵⁶ Porter, E. M., 1985.

⁵⁷ Normann, R. & Ramírez, R.

In addition to this, IKEA plays a major role in improving the business structure and manufacturing standards of its suppliers. Another example is Benetton; its operation builds almost entirely on external subcontracting with local producers in Italy, which are in many cases SMEs. On the market side Benetton sells and distributes its product through franchise holders, which allow a “just-in-time” flow from producers to the market with a very short production cycle. This leaves Benetton primarily as coordinator in the value chain where the physical flow of products never enters Benettons’ doors⁵⁸.

These new forms of relationships between buyers and suppliers demand much more overlapping links between companies and should not just be bound to the purchasing or marketing department of the companies; rather, there should be direct contact between people in these companies at whatever level is necessary, for example, staff in production, quality control and R&D⁵⁹. Close cooperation is in many cases the ground for implementing changes in production, for example, the implementation of the “just in time” system. Other changes involve a close working relationship with the suppliers as part of the programme such as TQM⁶⁰ in which the relationship with suppliers may be one of the key factors for success⁶¹. When companies are in the position where this new form of relationship between suppliers is in place and companies’ processes are integrated with suppliers’ processes, the competitive advantage can be significant. This will reflect in lower inventories, faster overall response time, higher quality and lower total cost⁶² (see Table V.4).

⁵⁸ Larsson, S.

⁵⁹ Steward, T.

⁶⁰ See for example Deming, W. D. & Juran, J. M.

⁶¹ Hayes, H. & Pisano, P. G.

⁶² Hayes, H. R., Wheelwright, C. S. & Clark, K. B.

Benefits from new suppliers' and customers' approach	
Benefits	Reasons
Lower inventories	Steady flow of supplies that you can trust No need for back orders in the company
Faster overall respond	Suppliers know the companies' needs and are willing to fulfil them Better information flow between companies Joint research programs
Higher quality	Less variance in the supplies Supplies fits companies' needs better Cooperation in quality control in the supplier's process
Lower purchase cost	Fewer suppliers Lower inspection cost
Lower total cost	By adding all this together the total cost goes down even though companies have to pay a higher price per volume than before.

Table V.4 Benefits from new suppliers' and customers' approach⁶³

Helper has found out in her research in the US automakers' industry where she studied changes in suppliers' relationships that *"once these relationships were built for the short term, suppliers were numerous, and competition was almost solely price-based. Now contracts are increasingly long term, sole sourcing is becoming more common, and competition is based on quality, delivery, and engineering as well as price"*.⁶⁴ In a similar way, research findings relating to the UK grocery supermarkets indicate that the tendency is for the supermarkets to try to cut down the number of suppliers and to build up long term relationships with suppliers⁶⁵. When a company implements these new forms of relationship with its suppliers and buyers the nature of the relationship moves from supply management to strategic partnership where the company has a long-term learning relationship with its suppliers and buyers⁶⁶. It can be argued that this form of suppliers' and buyers' relationship fits well in the definition of strategic alliances that was put forward in Chapter V.1.

V.2.2 Strategic Contribution of Strategic Alliances

The discussion above is more or less bound to vertical relationship in the value adding chain although strategic alliances can easily be horizontal. It

⁶³ This table is the authors' summation.

⁶⁴ Helper, S., page 15.

⁶⁵ Fearne, A. & Dedman, S.; Wysocki, F.A.; Cook, R.

⁶⁶ Lorenzoni, G. & Ornati, A. O.

can be argued that the same rationalisation can be used for the horizontal alliances as for vertical alliances when the basic condition is a win-win strategy based on cooperation and coordination. Contractor and Lorange have put forward a very good recapitulation of how strategic alliances can benefit companies. They maintain that, *“in broad terms, the joint venture, licensing, and other types of cooperating arrangements can achieve at least seven, more or less, overlapping objectives”*⁶⁷ that are listed in Table V.5.

Strategic Contributions of Joint Ventures	
Objectives	Strategic contribution
Risk reduction.	Product portfolio diversification. Dispersion and/or reduction of fixed cost. Lower total capital investment. Faster entry and payback.
Economies of scale and/or rationalisation.	Lower average cost from larger volume. Lower cost by using comparative advantage of each partner.
Complementary technology and patents exchanges.	Technological synergy. Exchange of patents and territories.
Co-opting or blocking competitions.	Defensive joint ventures to reduce competition. Offensive joint ventures to increase cost and/or lower market share for third company.
Overcoming government-mandated trade or investment barriers.	Receiving permit to operate as a “local” entity because of local partner. Satisfying local content requirements.
Facilitating initial international expansion of inexperienced firms.	Benefit from local partner’s know-how.
Vertical quasi-integration advantages of linking the complementary contributions of the partners in a “value chain”.	Access to materials, technology, labour, capital and distribution channels. Regulatory permits. Benefits from brand recognition. Establishing links with major buyers. Drawing on existing fixed marketing establishment.
<i>Economies of scope.</i>	<i>Possible to access to new markets Broader scope of products by using product from partner.</i>

Table V.5 Strategic Contributions of Joint Ventures⁶⁸

It is clear from Table V.5 that strategic alliances can benefit companies in many ways from reducing cost to getting access to new markets. Today’s business environment calls for strategy that builds on factors like low cost, high quality, innovation, spreading of risk, increased flexibility and quick

⁶⁷ Contractor, J. F. & Lorange, P., page 10.

⁶⁸ This table is direct from Contractor, J. F. & Lorange, P., page 10, except segment 8 that is the author’s input.

response to customer needs⁶⁹. The strategy of the 1970s and 1980s, where the emphasis was more on vertical integration, may, in this environment, be too costly and inflexible to respond to changes⁷⁰. Hence, companies have to think outside their own realm for resources and form strategic alliances with other companies. This can be a very good way for companies to respond to changes and strengthen their competitive status as well as reduce the risk of isolation.

Contractor and Lorange have the author's support in their opinion that it is equally important in companies' strategy to be able to collaborate with other companies as well as compete⁷¹. The principal objective of most of the strategic alliances between companies is almost always to obtain access to resources like technology, manufacturing, market, distribution and to service⁷². In addition to the direct benefits from these relationships between companies, there can also be hidden benefits. Because of the relationship with new partners, the companies have to look critically at their operations as well as receiving valuable new ideas from their partners. Alternatively, the new partner can make demands that stimulate improvements in the company⁷³.

V.3 Network perspective

In the academic literature on strategic alliances and networks there is an increasing emphasis on the need to shift the focus from viewing a company as a solitary unit to using a network approach where the emphasis is on the inter-organisational relationship of participants' companies⁷⁴. This means moving the focus towards a "network" perspective instead of "dominance" perspectives, such as the competitive analysis of Porter where outside companies are viewed as "extended rivals"⁷⁵ and the transactional cost

⁶⁹ Larson, S.

⁷⁰ Venkartraman, N.

⁷¹ Contractor, J. F. & Lorange, P.

⁷² Bidault, F. & Cummings, T.

⁷³ Bidault, F. & Cummings, T.

⁷⁴ Hellegren, B. & Stjernberg, T.; Axelsson, B.; Astley, W. G.; Contractor, J. F.; Walker, G.; Harrigan, R. K., 1985. ; Clegg, R. S.

⁷⁵ Johnston, R. & Lawrence, R. P.

theories that focus on the single relationship that a company has with its suppliers or customers⁷⁶. Hence, in these theories the dominance perspective is predominant, where the environment is viewed as totally competitive in the way that companies look at it as a whole and relate themselves to it as a whole⁷⁷. On the other hand, Walker states that “*an adequate understanding of a particular cooperative relationship can be achieved only by analysing the network of transaction in which the cooperative relationship is embedded*”⁷⁸. Axelsson claims that the environment should not be viewed as “*totally faceless and completely competitive*”⁷⁹ rather it should be viewed as a mixture of cooperative and competitive. Furthermore, Axelsson maintains that the best way to describe this is a “missing perspective” though it seems evident in newer academic research that this perspective is gradually emerging.⁸⁰

Hakansson and Johansson provide a basic structure of a model of industrial networks that could be said to be the basic for the “missing perspective” that Axelsson describes (see Figure V.5.). This model is also a helpful starting point in understanding the structure of the strategic alliances and the connection between the main variables in companies’ relationships. Although this model and discussion about the external relationship that companies have is framed in a network perspective, it will be argued here that it is well transferable to use for strategic alliances. Hellegren and Stjernberg define the concept “network” as a “*group of organisations that are related to each other, but have no common hierarchical structure of responsibility and only vague criteria for judging who is part of the network*”⁸¹. Alter and Hage provide a similar definition where “*Networks constitute the basic social form that permits inter-organizational interactions of exchange, concerted action, and joint production. Networks are unbounded or bounded clusters of organisations that, by definition, are*

⁷⁶ Axelsson, B.; Alter, C. & Hage, J. Osborn, N. R. & Hagedoorn, J.

⁷⁷ Pfeffer, J., 1987; Axelsson, B.

⁷⁸ Walker, G., page 228, 1988.

⁷⁹ Axelsson, B., page 193.

⁸⁰ Axelsson, B.

⁸¹ Hellegren, B. & Stjernberg, T., page 89.

*non-hierarchical collectives of legally separate units*⁸². In the same way strategic alliances cover a rather wide field of cooperative arrangement between companies as is discussed in Chapter V.1 and can be seen from the author's definition of the strategic alliances where *two or more companies cooperate together to attain shared strategic objectives*. From this definition it is clear though that strategic alliances should not be as vague a concept for the participant companies as is often the case with networks. Benassi claims that it is clear that network and strategic alliances are not interchangeable concepts⁸³. However, as in networks, participating companies in strategic alliances are separate units with no shared formal hierarchy. Hence it can be argued that strategic alliance is a part of the network that companies are involved in, or, as Lorenzoni and Baden-Fuller describe, that: strategic alliance is a strategy guided network⁸⁴.

The basic features of Hakansson and Johanson's model are actors, activities and resources⁸⁵ (see Figure V.5.).

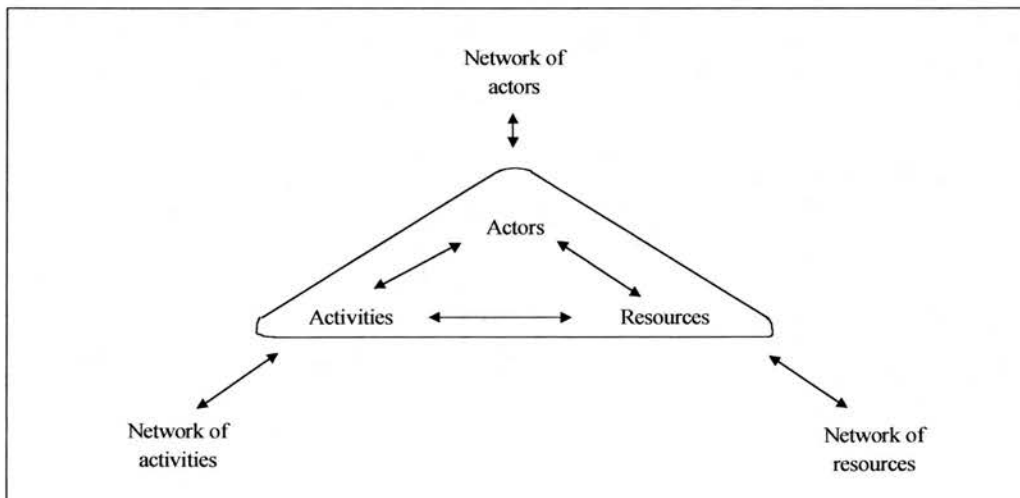


Figure V.5 Basic structural model of network⁸⁶

According to Hakansson and Johanson's model, actors are defined as "*those who perform activities and/or control resources*"⁸⁷, where individuals,

⁸² Alter, C. & Hage, J., page 46.

⁸³ Benassi, M.

⁸⁴ Lorenzoni, G. & Baden-Fuller, C., page 146.

⁸⁵ Hakansson, H. & Johanson, J., page 28, 1992.

⁸⁶ Hakansson, H. & Johanson, J., 1992.

⁸⁷ Hakansson, H. & Johanson, J., page 28, 1992.

groups of individuals, parts of firms, firms, and groups of firms can be actors. Furthermore Hakansson and Johanson claim that actors have five main characteristics; first they perform and control activities, secondly actors develop relationships with each other through exchange processes, thirdly they base their activities on control over resources, fourthly actors are goal oriented and finally actors have different knowledge about activities, resources and other actors in the network⁸⁸. According to this actors can be on different organisational levels inside the participant companies.

According to Hakansson and Johanson activities “*occur when one or several actors combine, develop, exchange, or create resources by utilising other resources*”⁸⁹. They split the activities into two groups; firstly, the transformation activities that are always directly controlled by one actor, and secondly, transfer activities that transfer direct control over a resource from one actor to another⁹⁰. Activities are linked together in various ways, some tightly coupled while others are more loosely coupled. In addition, activities are performed by actors, and resources are controlled by actors either individually or jointly. The nature of resources in networks is heterogeneous and Hakansson and Johanson categorise them in the same way as the activities, which is that transformation resources are needed to perform transformation activities and transform resources are required to perform transformed activities⁹¹.

Axelsson claims that these three factors (actors, activities and resources) are closely connected and can cause conflict and power struggle in companies' relationships such as when “*actors in different levels, controlling different resources and being involved in different activities may differ in their intentions and perceptions....*”⁹². Benassi claims that the network perspective, which requires a holistic approach and is more than just a sum

⁸⁸ Hakansson, H. & Johanson, J., 1992.

⁸⁹ Hakansson, H. & Johanson, J., page 30, 1992.

⁹⁰ Hakansson, H. & Johanson, J., 1992.

⁹¹ Hakansson, H. & Johanson, J., 1992.

⁹² Axelsson, B., page 199.

of “*dyadic relations*”⁹³, is very useful in studying strategic alliances and offers a very useful insight into the alliances, which with the other perspective would be difficult⁹⁴. It is the author’s conclusion that it is essential to recognise these factors and their relationship to understand strategic alliances and the relationship that companies have with each other therein. In the same way it is necessary to understand the external demands that strategic alliances and other forms of cooperative relationship make as it is necessary to understand the demands that this external relationship makes inwards on the structure and governance of participant companies. This can be supported with Nohria where he claims that the main difference between the Porter’s framework of analysing industry and the network perspective is “... *that greater attention is paid in the network perspective to the overall pattern of relationship among firms in the industry, an issue that receives short shrift in Porter’s framework*”⁹⁵.

This view of the companies’ environment where the company is embedded in it, and the emphasis on the patterns of relationship, is perhaps one of the weaknesses in the network perspective at the same time as being its main strength. The network perspective can cover almost all relationships between companies. In literature about the network perspective it is common that all relationships between companies, both formal and informal, as well as both personal and on business level, are covered. This is a great difference from the economical view of the transactional cost theories where the transactional cost is almost the only criteria used to study the relationship between the companies. This wide view of the network perspective makes the literature often unclear and badly focused which is in many cases understandable considering it is described as an “emerging perspective” as Axelsson claims⁹⁶. This is supported by Nohria where he claims that in some cases the network perspective is applied so loosely that it stops having any meaning in describing companies relationships⁹⁷.

⁹³ Dyadic relationship means relationship that are built on two companies.

⁹⁴ Benassi, M.

⁹⁵ Nohria, N., page 6.

⁹⁶ Axelsson, B.

⁹⁷ Nohria, N.

Despite this it is the authors conclusion that the network perspective offers a necessary view over the companies environment to understand the nature of the networks and their development. To conclude this part about the network perspective it is appropriate to quote Alter and Hage. They claim that the “...it is these cooperative behaviours-the growing number of partnerships, alliances, joint ventures, consortia, obligational and systematic networks-that represent a stunning evolutionary change in institutional forms of governance”⁹⁸. Furthermore they predict that the inter-organisational network will be the future institution and this new institutional form will increasingly replace both markets and hierarchies as a governance mechanism⁹⁹. Whether that is the case will not be evaluated here but clearly the network perspective gives new insight into the institutional environment of companies where the emphasis is that firms are embedded in the environment¹⁰⁰. This gives a new dimension to the traditional perspective of the transactional and competitive perspectives and offers opportunities to better understand the strategic alliances and other cooperative arrangements that companies participate in.

V.4 Governance of Strategic Alliances

Current literature on strategic alliances has undervalued the importance of the management aspect of strategic alliances and put much more emphasis on the planning, partner selection and formal agreement of the alliances¹⁰¹. The reported high percentage of failures of strategic alliances demonstrates possible operating problems suggesting that the management aspects are not fully understood¹⁰². Furthermore it has been pointed out that special abilities are required of managers in strategic alliances as opposed to those necessary for hierarchically structured firms which pursue a “go it alone strategy”¹⁰³. These abilities are based on the fact that the managers often

⁹⁸ Alter, C. & Hage, J., page 12.

⁹⁹ Alter, C. & Hage, J.

¹⁰⁰ Axelsson, B.

¹⁰¹ Benassi, M.

¹⁰² Parker, N.

¹⁰³ Hasting, C., page 30.

lack the formal authority in the strategic alliances that they have in their own company, which leads to more emphasis on the social skills of the managers when they enter strategic alliances than in single company. In addition to literature on the governance of strategic alliances, lessons will be drawn from the literature on networks as well as the network perspective in this section. The discussion starts by looking at the administrative mechanisms of strategic alliances leading to the more internal organisational demands of such relationships. The final discussion concerns power that more or less overlaps other elements of the governance of strategic alliances.

V.4.1 Administration mechanism

Yves L. Doz pointed out that the “*operating interfaces between the two partners cannot be left to chance and to ad hoc adjustment*”.¹⁰⁴ Instead, a clear internal organisational relationship, as exists in strategic alliances, demands some kind of administrative mechanism¹⁰⁵ to be able to share information and knowledge as well as to coordinate activities¹⁰⁶ with the overall aim of making the strategic alliances efficient and competitive. In the formally described organisation form that is the “market” and “hierarchy”, the administrative control and coordination is achieved through the “hierarchy” controlled process of vertically integrated firms or the invisible hand of the “market” where the price and competition are the most relevant factors¹⁰⁷. In strategic alliances there is no formal authority or hierarchy to manage or coordinate inter-organisational activities, instead the companies have to cooperate to be able to coordinate their activities¹⁰⁸.

The network perspective put forward by Hakansson and Johanson presents the relationship between actors and activities and/or resources (as is seen in Figure V.6)¹⁰⁹.

¹⁰⁴ Doz, L. Y., page 337.

¹⁰⁵ Axelsson, B.

¹⁰⁶ Johnston, R. & Lawrence, R. P.

¹⁰⁷ Axelsson, B.

¹⁰⁸ Hellegren, B. & Stjernberg, T.

¹⁰⁹ Hakansson, H. & Johanson, J., page 36, 1992.

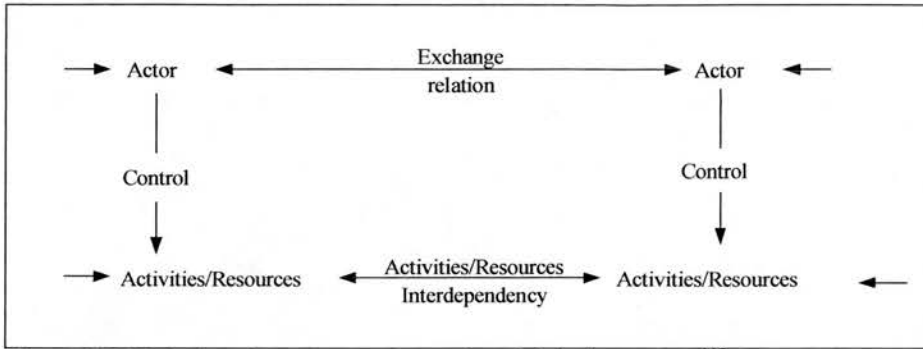


Figure V.6 Relations between actors and activities/resources¹¹⁰

In this model actors connect to actors through an exchange relation that Hakansson and Johansson claim is the basic element of the network, where this relationship suggests some kind of mutuality through involvement of actors in giving away and receiving from one another¹¹¹. Actors then have control over certain activities and resources that are connected to activities and/or resources of other actors through interdependence. Hakansson and Johansson claim that the exchange relationship between actors is some kind of mutuality of exchange that is not just an economic dimension but also a knowledge and value dimension¹¹². In the same way dependency or interdependency is clearly at the centre of this model. Interdependency in both activities and resource indicates that actors have to depend on other actors for some activities and resources. Smith and Helleman point out that dependency is probably strongest between actors that are located close to each other in the network, for example involving a common actor, activity or resources¹¹³. This could be the case for companies connected to each other in the value chain such as where they are not only dependent on the next company on products, but rather on their resources and activities. It will be argued here that actors depend on each other concerning control due to the fact that individual activities and resources are partly dependent on other actors and their control.

What is missing from this model as presented in Figure V.6 is how these inter-activities of actors, activities and resources are managed. Academics

¹¹⁰ Hakansson, H. & Johanson, J., page 36, 1992.

¹¹¹ Hakansson, H. & Johanson, J., 1993.

¹¹² Hakansson, H. & Johanson, J., 1993.

¹¹³ Smith, P. C. & Laage-Helleman, J.

seem to be unanimous that the key to the administrative mechanisms in networks and strategic alliances is coordination¹¹⁴. What is often not as clear is what is involved in coordination and how this coordination is achieved. Lundgren claims that in the network perspective “*coordination refers to the organising of function and flows, that is, activities and relationships, within a network, to increase the effectiveness of activity cycle*”¹¹⁵. It can then be argued that, in its simplest form, coordination is meant to coordinate the flow of activities and resources between actors in the network.

One of the influencing factors on the administrative mechanism used in the alliances is the structure and scope of the alliances. According to Devanna and Tichy “*the great majority of inter-firm associations since the 1980s have tended to be less formal in structure and more specific in scope and purpose*”¹¹⁶. This suggests that the alliances have to depend more on the informal coordination structure than formal coordination. One aspect of the formal structure is the establishment of formal contracts. It has been increasingly pointed out that the establishment of formal contracts, and especially of the external law-protected kind, is costly and possibly self-defeating in integrative games¹¹⁷. Grandori claims that the “*establishment of formal contracts entails a variety of transaction costs, including set up and administration costs; search, decision and negotiation costs; and possibly costs of loss of cooperative atmosphere*”¹¹⁸. Much rather than building the alliance on formal contract, Lorange and Roos say that in their experience “*the foundation of successful strategic alliances is laid during the initial formation process. It is at that stage that the analytical and political dimensions and issues have to be dealt with in such a way that clear and realistic intents are established and that the foundation for trust and behavioural consonance is laid*”¹¹⁹. Killing found out in his research on

¹¹⁴ Alter, C. & Hage, J.; Hellegren, B. & Stjernberg, T.; Jarillo, C. J.

¹¹⁵ Lundgren, A., page 157.

¹¹⁶ Devanna, A. M. & Thichy, N., page 458.

¹¹⁷ Grandori, A.

¹¹⁸ Grandori, A., page 910.

¹¹⁹ Lorange, P. & Roos, J., page 28.

companies' experience of strategic alliances that the "*key to success in alliance building is to create an alliance that is simple enough to be manageable*"¹²⁰. Furthermore he claims that complexity leads to failure¹²¹.

V.4.1.1 Coordination

Coordination is one of the essences of the organisational structure of companies, as can be seen from the definition of the formal organisational structure of companies. This definition is that organisational structure is the "*rational coordination of people, information and technology around some common purpose to produce an output*"¹²². Organisational structure can also be split into two structures¹²³. These are "*basic structure which allocates and co-ordinates people often through job descriptions, organisational chart and resource; and the operating structure which specifies more detailed activities and forms of behaviour, such as those embodied in performance review, work plans and communication, financial or reward systems*"¹²⁴. It can be argued that the inter-organisational relationship between companies in strategic alliances goes mainly through the operating structure due to the fact that the participating companies have no shared hierarchy or structure, so the basic structure is separated.

Lundgren points out that in the network perspective the coordination is not solely achieved through planning and control, rather that coordination in network perspective is a process of mutual adaptation and learning¹²⁵. This is one of the essences of the network perspective, that is, this process of mutual adaptation and learning that changes the structure of the networks as well as affects the distribution of power in the network¹²⁶. Furthermore Lundgren claims that a perfectly coordinated and balanced network is a

¹²⁰ Killing, P. J., page 55.

¹²¹ Killing, P. J.

¹²² Devanna, A. M. & Thichy, N., page 457.

¹²³ Thompson, P. & McHugh, D., page 156.

¹²⁴ Thompson, P. & McHugh, D., page 156.

¹²⁵ Lundgren, A.

¹²⁶ Lundgren, A.

static network¹²⁷. On the other hand a network that is unbalanced is constantly adjusting and learning, and this is the driving force behind development and changes in the network¹²⁸.

What emerged from the literature about networks, strategic alliances and traditional organisation is that coordination is achieved through a mixture of formal and informal mechanisms. An example can be taken from Alter and Hage who found that companies tend to use mainly three methods of achieving administrative coordination in alliances¹²⁹:

- **Written rules and contract** were used when outcomes were predictable.
- **Personal coordination and communication** were used when work volume was heavy and work process brief.
- **Group decision making** by administrators occurred where the task scope was broad.

In similar ways, Benassi, in his research on strategic alliances, found out that coordination is often characterised by¹³⁰:

- **Information openness** among partners so that different communication channels can be used according to the needs of the strategic alliances.
- **Mutual support** by actors participating in the strategic alliances, which often can outflank obstacles to which each partner may be subject
- **Personal networks** arising among actors involved in the alliance.

A final example can be taken from Lorenzoni and Ornati, who in their research on growth of SMEs found out that companies tend to use unconventional mechanisms of coordination while organisational design matures¹³¹. What emerged from their research includes:

- **Trust:** among the partners: which is a priority and is confirmed by all scholars analysing reticular forms of organisations
- **Reciprocity:** operationally reinforcing the trust effect as a lubricant of interfirm relationships.
- **Mutual adjustment:** accepting problems and views of the partner and managing to solve them.

¹²⁷ Lundgren, A.

¹²⁸ Lundgren, A.

¹²⁹ Alter, C & Hage, J., page 171.

¹³⁰ Benassi, M., page 103.

¹³¹ Lorenzoni, G. & Ornati, A. O., page 45.

- **Multiple lines relationship** (horizontal, vertical and lateral): developing intelligence, information and reciprocal influence circulating on multiple tracts.

It is clear from these three examples that the emphasis is on the informal or personal coordination with the exception of Alter and Hage who mention written rules and contracts as one option. The choice of coordination mechanisms in strategic alliances depends heavily on the nature of the relationship, the interaction between participating companies and the number of participating companies. In many cases in the literature on network or strategic alliances, examples are taken from a dyadic relationship involving only two companies. Benassi points out three types of relationship as can be seen in Figure V.7. First are the dyadic relations of two companies, second are convergent relations and third are systematic relations¹³².

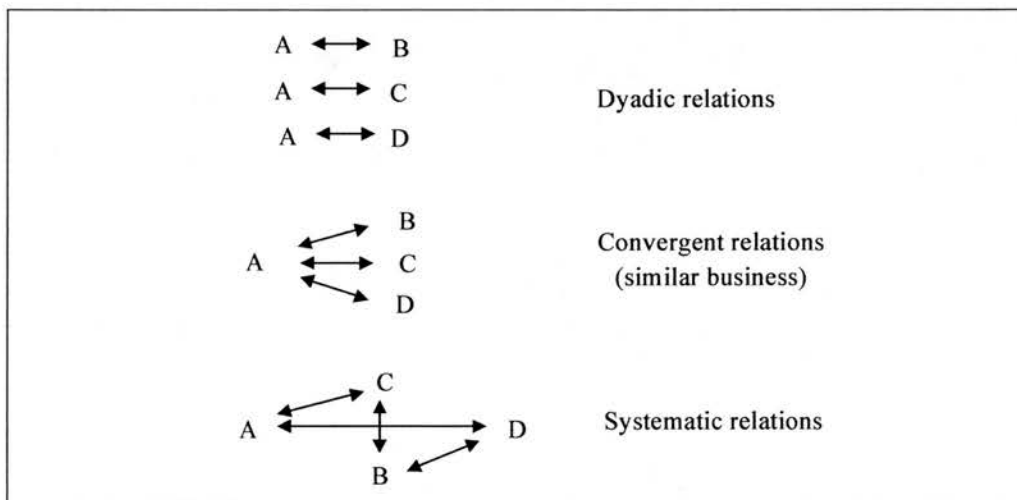


Figure V.7 Different form of relations between companies¹³³

It could be suggested that in the real world more types of relationship will occur, for example a mixture of convergent relations and systemic relations. Other influencing factors on the coordination include the degree of interaction and dependency. This can be reflected in that companies with little interaction and dependency can get away with informal mechanisms

¹³² Benassi, M.

¹³³ Benassi, M., page 103.

while companies with greater interaction and dependency would need more formal mechanism and structure¹³⁴.

V.4.1.2 Strategic centre

One way of coordination that is increasingly discussed in the academic literature on strategic alliances is the central or focal firm that acts as a strategic leader for the network. Lorenzoni and Baden-Fuller say that one of the essences of successful strategic alliances is the need to be strategically guided and a network that is not guided strategically by a “centre” is increasingly unable to meet the demanding challenges of today’s markets¹³⁵. Lorenzoni and Baden -Fuller take examples from the Italian textile industry mainly from Benetton, which has built up a vertical network in the value adding chain through many small and medium size companies. They claim that one of the conditions for success is to have one central firm that strategically guides the network of participating companies. Jarillo similarly emphasised the role of a “hub” firm *“which is often the firm that established the network and takes a pro-active attitude in taking care of it”*¹³⁶. Easton has pointed out the importance of a “focal” firm, which is the firm that has connections with other firms in the network¹³⁷. This idea of a central firm has also been phrased as a “constellation” form of organisations where the emphasis is on the leadership of a central firm controlling critical competence and uncertainties as a coordination mechanism¹³⁸. Lorange and Roos on other hand put emphasis on the strategic planning and control as a process to coordinate activities in the alliances and avoid information asymmetry¹³⁹.

In this discussion about strategic centres, hub firms, constellations and focal firms it is obvious that the emphasis is on the need for one company to take care of leading the alliances. In many senses it moves the emphasis from

¹³⁴ Easton, G.

¹³⁵ Lorenzoni, G. & Baden-Fuller, C.

¹³⁶ Jarillo, C. J., page 32.

¹³⁷ Easton, G.

¹³⁸ Grandori, A.

¹³⁹ Lorange, P. & Roos, J.

the idea that coordination can be achieved through some grassroots movement¹⁴⁰ to more formal methods of coordination. By formal methods one does not mean traditional methods of headquarters' governance and their domination, rather that the centre has a strategic role to lead and be a leader in forming strategy and framework that one participating companies can work inside with the freedom of being individual companies. Lorenzoni and Baden-Fuller frame this by claiming that the strategic centre has three main roles: that is, first to be a creator of value for its partners, second to be a leader, rule setter and capability builder, and third to simultaneously structure and strategize the network¹⁴¹. In the cases that Lorenzoni and Baden-Fuller examined, the strategic centre is most appropriate where the network covers multiple stages in the value adding chain where many companies are involved and are considered to be an alternative to large integrated multi-market organisation¹⁴². Lorenzoni and Baden-Fuller emphasised that the strategic centre should not just coordinate and rule the network, but also create an atmosphere where the participating companies can be creative and the network flexible¹⁴³.

In this discussion about the role of a centre, solid lessons can be learned from multi-business firms that base their governance, often through a centre, and usually in the form of headquarters. Campbell, Goold and Alexander have in their research on corporate strategy found that parent companies in many cases tend to destroy the value of their participating business units rather than create value¹⁴⁴. The main reason for the value destruction is that the parent companies exercised too much centralisation of their business units in matters such as business development, strategy, and control. The value destruction occurred when the headquarters acted as if they knew how to do individual things better than the business units, leading to ineffective business decisions and strategy because of the great emphasis on

¹⁴⁰ Thompson, P. & McHugh, D.

¹⁴¹ Lorenzoni, G. & Baden-Fuller, C.

¹⁴² Lorenzoni, G. & Baden-Fuller, C.

¹⁴³ Lorenzoni, G. & Baden-Fuller, C.

¹⁴⁴ Campbell, A., Goold, M. & Alexander, M., 1994.

centralisation and the controlling role of headquarters¹⁴⁵. It is clear from the example Campbell et al take that the basis for successful value creation through parenting is a much more decentralised system where the participating companies have freedom to develop their own business with the help and support of the parent companies. Then the parents' companies act much more as an overall strategic leader and supporter, rather than being involved in detailed strategy and business decisions¹⁴⁶, which is in many ways similar to the role of the central firm in the case of Lorenzoni and Baden-Fuller.

V.4.2 Organisational demands of Strategic alliances

Interactive relationships between companies challenge in many ways the traditional view of the organisational structure of companies built on hierarchy. The strategic alliances demand much more of the participant companies in terms of sharing information, having good communication and making faster decisions than single companies. This calls for changes of emphasis, such as on speed, innovation, learning, flexibility and processes for absorbing the new information. Ghoshal and Bartlett pointed out that companies have to see themselves not as a hierarchy but rather as a portfolio of dynamic processes. They found out in an examination of twenty Japanese companies that when the managers looked at their companies they saw processes not structure¹⁴⁷. The processes they saw were:

1. **Entrepreneurial process** that provides creative and entrepreneurial characteristics in front-line managers.
2. **Competence building process** that builds competence across the company's internal organisational boundaries.
3. **The renewal process of a company's core organisational processes** that promote continuous renewal of the strategies and ideas that drive the business.

Processes in companies reach out to both suppliers and customers and it is important that this flow is as good as possible. Bartlett and Ghoshal also place emphasis on the transitional organisation that is, in a way, similar to strategic alliances in that the flow in the organisation is crucial¹⁴⁸. The flow

¹⁴⁵ Campbell, A., Goold, M. & Alexander, M., 1994.

¹⁴⁶ Campbell, A., Goold, M. & Alexander, M., 1994.

¹⁴⁷ Ghoshal, S. & Bartlett, A. C., page 89.

¹⁴⁸ Bartlett, A. C. & Ghoshal, S., 1991.

they talk about is threefold: firstly there must be a flow of parts, components, and finished goods; secondly there must be management of the flow of funds, skills, and other scarce resources among units; thirdly there must be a link between intelligence, ideas and knowledge that is central to innovation and learning capabilities.

In a similar way David Ulrich, the editor of "Human Resource Management", pointed out three levels of boundaries that can exist in companies. He states that it is essential to lay emphasis on overcoming the negative characteristics of the traditional hierarchy structure in companies¹⁴⁹. The first boundary he talks about is the vertical boundary caused by the number of layers in the hierarchy. This means that in the decision making process, communication and information sharing may suffer from the number of layers in the organisational structure. The second boundary is the internal horizontal boundary between the departments or those that function within the organisational structure. These boundaries often cause conflict between departments, for example between production and marketing. This conflict is often due to the separation of departments and because communication, information and decisions have to follow the hierarchy. This can take a long time and often misses the point when it finally reaches the person who needed the information or decision in the first place. The third boundary is the external horizontal (or vertical) boundary that can occur in the value chain. Ulrich claims that this is the most difficult boundary to break because it needs a fundamental change in the concept and definition of the organisation¹⁵⁰. He goes on to say that these are also the most important boundaries to break in order to make strategic alliances successful. Similar focusing on processes is found in the theory of TQM and Reengineering where great emphasis is placed on working with both suppliers and customers to improve the processes and their flow¹⁵¹.

¹⁴⁹ Ulrich, D.

¹⁵⁰ Ulrich, D.

¹⁵¹ See for example Davenport, H. T., Juran, M. J. & Deming, W. D.

This emphasis on process and flow without barriers between companies reflects well the contradiction between the network perspective and the dominating perspectives where the bargaining power over external relationship is seen as crucial for the companies' competitive stance¹⁵². A prime emphasis in the new literature on the organisational structure of companies points in the same direction. If companies want to be competitive they have to break down boundaries and barriers, both internally and externally. Different terminology has been used to explain the new emphases in organisational structure of companies such as innovation¹⁵³, flexibility, strategy and production¹⁵⁴, lean organisation¹⁵⁵, learning organisation¹⁵⁶ and trust¹⁵⁷. These new emphases on organisational structure have been described as organisational structure without boundaries. What is crucial in the new organisational structure is the operating part (often called the "softer" part) of the organisational structure. These softer issues are, for example, the internal culture, value system, information system, learning, teamwork, and communication between people¹⁵⁸. Also, the competitiveness of the organisational structure is built on speed and learning rather than on specialisation and economy of scale¹⁵⁹. In order to highlight these two systems a comparison is made in Table V.6. It has to be recognised that this is a comparison of two extremes, which have lots of different combinations or forms in between.

¹⁵² Johnston, R., & Lawrence, R. P.; Pfeffer, J., 1987; Axelsson, B.; Alter, C. & Hage, J.

¹⁵³ Ball, A. D. & McCulloch, H. W. Jr., page 689.

¹⁵⁴ Hayes, H. & Pisano, P. G., page 78.

¹⁵⁵ Burgess, F.T., page 23.

¹⁵⁶ Garvin, A. D., page 78.

¹⁵⁷ Handy, C., page 43.

¹⁵⁸ Stewart, T.

¹⁵⁹ Devanna, A. M. & Thichy, N.

Comparison of the old and new approach to management	
Hierarchy, Mechanism Structure	Network, Learning Structure
Hierarchy	Network
Control and bureaucracy	Flexibility
Knowledge and refreshers course are just for specialists	Refresher courses and knowledge are for all employees
One-sided communication after the hierarchy	Double-sided communication and direct
Decision lies high in the hierarchy	Decentralisation and decision at the workplace
Management build up on skill and knowledge	Emphasis on leadership
Management from the top moving downwards	Direct leadership
Specialisation	Knowledge and education to every employee
Small changes in the system	Continual development of the system

Table V.6 Comparison of the old and new approach to management¹⁶⁰

Hierarchical structure is usually associated with large and vertical firms, and must be recognised as probably the most effective structure when the product is standardised, produced in high volume, and can remain unchanged over a long time period¹⁶¹. Furthermore, Alter and Hage maintain that the products' life cycle is increasingly getting shorter, leading to an increased disadvantage of having a large organization with hierarchical structure, due to difficulties in coping and adjusting to rapid changes in the market conditions¹⁶². Hasting points out as well that the old hierarchy system has serious problems in slow and inefficient communication, and its culture "*generally teaches people to keep their heads down to limit their expectations*"¹⁶³. Large vertically integrated companies tend to share as little knowledge as possible, and in many cases, they view their external relationship in accordance to the dominant competitive perspective and concentrate on having bargaining power over them¹⁶⁴. In addition the bureaucratic structure results in managers that lack knowledge over activities along the value adding chain¹⁶⁵. An example to support this can

¹⁶⁰ Built on table putted forward of Devanna, A. M. & Tichy, N., page 458.

¹⁶¹ Alter, C. & Hage, J.; Lorenzoni, G. & Ornati, A. O.

¹⁶² Alter, C. & Hage, J.

¹⁶³ Hasting, C., page 3.

¹⁶⁴ Johnston, R. & Lawrence, R. P.

¹⁶⁵ Johnston, R. & Lawrence, R. P.

be taken from an interview with a CEO of a small company, which was in a strategic alliance with a larger company. He said *"I found myself unwillingly in the position to arbitrate between units of my partner. I had more information than any of their units had, they did not talk among themselves, but each talked to me!"*¹⁶⁶.

This suggests that there are some internal organisational barriers in the hierarchical structure indicating that companies with such structure could have serious problems in participating in successful strategy alliances. These barriers are both connected to the visible organisational structure of the companies as well as to the more invisible "softer" part which includes culture and communication. In the visible part these barriers could be built in factors such as many levels in the structure, numbers of departments and bureaucratic systems¹⁶⁷. The "softer" part includes for issues such as culture, trust, attitude, value system, information system, learning, teamwork, and communication between people¹⁶⁸. Hasting claims that it is even more important to tackle the softer barriers such as communication and culture to make companies capable of coping with inter-firm-relationships¹⁶⁹.

V.4.2.1 Culture

Thompson and McHugh define corporate culture as *"the way that management mobilises combinations of values, language, rituals and myths"*¹⁷⁰. The corporate culture can, therefore, be seen as a key factor in the commitment and enthusiasm of the work force that is working for the company so that they feel that they are working for something worthwhile. Robert D. Hass, CEO of Levi Strauss said in an interview *"that in the future the competitive advance of companies would not be their product or technology but, **who** is going to do the work, **how** they will do it, **why** they*

¹⁶⁶ Doz, L. Y., page 327.

¹⁶⁷ Hasting, C.

¹⁶⁸ Stewart, T.

¹⁶⁹ Hasting, C.

¹⁷⁰ Thompson, P. & McHugh, D., page 198.

will do it and how valuable will the work be to them"¹⁷¹. Corporate culture is very different between companies and it is, therefore, difficult to generalise. Corporate culture is likely affected by factors such as nationality of the company, size, organisational structure, the company's management style and last but not least the aims of the company. Examples of different corporate culture are often taken from US and Japanese companies. In Japan the management builds on attributed values like teamwork, trust, consensus, shared responsibility, loyalties, long term employment, stability, commitment and tactics such as just-in-time and quality improvement throughout the value chain¹⁷². At the same time the culture of US companies and many companies in the western world has been built around individualism, specialisation and rapid change of the employees. Hence, there have been signs that employees' loyalties and commitment to the organisation are declining in US and other western countries¹⁷³. These differences in culture can easily lead to difficulties in managing strategic alliances leading to irritation amongst managers, poor communication, slow decision processes and misunderstanding between companies, which can lead to a lack of trust between the companies. It is important to understand and respect the national culture in the country where the alliance is taking place in order to avoid unnecessary misunderstandings and irritating conflict, which can jeopardise the alliances¹⁷⁴. Differences in culture can also exist between companies of different size and even between companies of similar size that are in similar businesses. Even in the same company there can be some cultural difference, for example, the culture in the marketing division and the product division. Thompson and McHugh pointed out that it is important for all kinds of organisation to create a corporate culture that is resonant with the overall goals of the company¹⁷⁵. They also emphasise that it is even more important to do this for consensual groupings. Hence, it would be a mistake if managers of strategic alliances,

¹⁷¹ Webber, M. A., page 30.

¹⁷² Dunning, H. J.

¹⁷³ Nam, H. S.

¹⁷⁴ Nam, H. S.; Doz, L. Y.

¹⁷⁵ Thompson, P. & McHugh, D.

paid no attention to the cultural differences between companies. Furthermore the author concludes that it is even more important to build up a culture that supports the behaviour, attitude and trust that the company needs in order to build successful alliances.

V.4.2.2 Trust and Attitude

Trust has for a long time been considered to be one of the key elements in successful strategic alliances¹⁷⁶. In the transaction theory and competitive analysis of Porter lack of trust is one of the key element in companies' relationships leading to a fear of depending too heavily on single or few suppliers because they could exercise their bargaining power to get a dominant position and by that heighten the transactional cost¹⁷⁷. On the other hand, trust and positive attitude towards cooperation is one of the key elements in developing successful strategic alliances¹⁷⁸. Lundvall points out that trust cannot be bought and building trust on formal contracts is expensive and would heighten the transaction cost rather than lowering it, which is often the objective in cooperating¹⁷⁹. In order to build up trust, a positive attitude, especially by top managers, towards strategic alliances is crucial. In similar ways Alter and Hage claim that willingness to cooperate is one of four basic conditions of building up successful alliances¹⁸⁰. Willingness to cooperate, positive attitude and trust do not come without effort, so top managers and leaders of participating companies must show in their behaviour that they can be trusted and have a positive attitude towards the alliances. Leavitt and Bahrami point out that in the long run, behaviour tends to go in line with attitude so to change behaviour it is necessary to attempt to change attitudes¹⁸¹. Public commitment is perhaps the most important aspect of gaining a positive attitude towards changes in organisations. In order to achieve this commitment, the public (staff in this

¹⁷⁶ Alter, C. & Hage, J.

¹⁷⁷ Jarillo, C. J.; Lazerson, M.; Johnston, R. & Lawrence, R. P.

¹⁷⁸ Alter, C. & Hage, J.; Lundvall, B-A.

¹⁷⁹ Lundvall, B-A.

¹⁸⁰ Alter, C. & Hage, J.

¹⁸¹ Leavitt, J. H. & Bahrami, H.

instance) needs to have some visible role model to take a stand for the changes and to act as a driving force for them¹⁸². It is, therefore, vital in bringing about changes, such as cultural or organisational, that the top managers' team has the right attitude towards them and acts as a role model. This is because individuals on the team and as a whole can transfer the company's administrative heritage by being role models to build a new management perspective and capability within the company¹⁸³. This is even more important in strategic alliances than in changes inside one company, as strategic alliances call for a new view of how the business is operated, because in alliances people and companies often give up private resources to gain access to collective ones¹⁸⁴.

V.4.2.3 Power

Power is a central issue in almost all perspectives and theories in studying organisations and cooperation between them, although different perspectives have different approaches and views about power¹⁸⁵. In a simple way, power has been defined, as *"the ability of A to get B to do something that B would not otherwise do, despite any resistance"*¹⁸⁶. Pfeffer's definition of power is similar where he states *"power is the potential ability to influence behaviour, to change the course of events, to overcome resistance, and to get people to do things that they would not otherwise do"*¹⁸⁷. Foucault, the French philosopher, defines power in his early work "Madness and Civilisation" with a negative perspective that *"power is to force people to do something that they would not do and would resist doing"*¹⁸⁸. In his later works, as in "Discipline and Punish", he admits that his earlier view on power was too narrow and negative. He admits that power does not only

¹⁸² Thompson, P. & McHugh, D.

¹⁸³ Barlett, A. C. & Ghoshal, S., 1991.

¹⁸⁴ Alter, C. & Hage, J.

¹⁸⁵ Axelsson, B.

¹⁸⁶ Thompson, P. & McHugh, D., page 133.

¹⁸⁷ Pfeffer, J., page 30.

¹⁸⁸ Foucault, M., page 119, 1980.

weigh on us as a force, but it has also a positive effect, which causes people to be productive in modern societies¹⁸⁹.

In order to make power more visible in the companies, it is helpful to study how it can be located inside the company. The formal power structure is the organisational structure in the companies that was designed with formal authority in mind¹⁹⁰. The traditional form of organisation, that is, the hierarchy, makes it simple to plot out the formal authority in the company. In many cases, this structure does not tell the observer about all power in the company. There may be other forms of countervailing power that may overwhelm the formal authority. This is because it takes more than rank and role to influence people¹⁹¹. As Pfeffer says "*politics and influences are the processes, the actions, the behaviour through which this potential power is utilised and realised*"¹⁹². According to this, it is very possible that people who have no formal rank in companies can have more power than those who have the formal authority. These can be people who have knowledge, skill, access to information and social respect from others inside or outside the company. In addition to this, in the more modern organisational structure based on teamwork, processes, and leaner structure, the power is spread through the company and is less visible than before¹⁹³. This leads to the fact that people can use resources as a way to execute power over people who do not have the same resources, and where people can use access to resources to gain more power in the organisation¹⁹⁴.

Pfeffer claims that power in networks often arises from centralised control or coordination over other participants in the network¹⁹⁵. In the same way, individuals inside a company can use control of resources to gain or maintain power. Lorenzoni and Baden-Fuller claim that "*to maintain the*

¹⁸⁹ Foucault, M., 1991.

¹⁹⁰ Leavitt, J. H. & Bahrami, H.

¹⁹¹ Leavitt, J. H. & Bahrami, H.

¹⁹² Pfeffer, J., page 30, 1992.

¹⁹³ Connolly, E. W.

¹⁹⁴ Thompson, P. & McHugh, D.

¹⁹⁵ Pfeffer, J., 1987.

¹⁹⁶ Lorenzoni, G. & Baden-Fuller, C., page 153 - 154.

balance of power in the network, all central firms retain certain activities. The control of the brand names and development of the systems that integrate the network are two activities that give the organisation a pivotal role and allow it to exercise power over the system"¹⁹⁶. Lorange and Roos mention that companies, and mainly the central or focal company, in strategic alliances tend to have some "black box" where they protect unique proprietary skills and know-how from other companies in the case of break-up of the alliances¹⁹⁷. Doz found out, in his research of technical alliances between large and small companies, that the small firms almost always try to retain control over the technology because it is their only bargaining strength¹⁹⁸. At the same time the small firms were afraid that the bigger firms would take detrimental action that the small firms could not resist and could put their future in jeopardy¹⁹⁹. This detrimental action could be taking over the small firms or by insisting that more capital was put into the alliances than the small firm could afford. This would lead to a take-over by the bigger firm. On the other hand, Fearne and Dedman found out in their research of supermarkets that with added concentration among them and growing power in the supply chain they became increasingly dependent on fewer and larger suppliers²⁰⁰. Fearne and Dedman phrase this as "power paradox" due to the paradox of the powerful position of the supermarkets in the value chain compared to the suppliers²⁰¹. Lorange and Roos point out that there is too often a tendency in strategic alliances to under-allocate critical resources and/or to commit resources only on general terms leading to the danger of unsuccessful alliances due to lack of trust and insufficient dedication of participating companies²⁰². Lorenzoni and Baden -Fuller claim in a similar way that successful central firms tend to stick to very few core skills and assets, and handout as much of the resources as possible,

¹⁹⁷ Lorange, P. & Roos, J.

¹⁹⁸ Doz, L. Y.

¹⁹⁹ Doz, L. Y.

²⁰⁰ Fearne, A. & Dedman, S.

²⁰¹ Fearne, A. & Dedman, S.

²⁰² Lorange, P. & Roos, J.

making the alliances much more value adding for the participating companies²⁰³.

Power can also be related to individual persons inside companies; for example, the CEO can see alliances and collaboration as a loss of power leading to a loss of direct authority (visible power). Lorange and Roos call this power that can often hinder the alliances “kingdom mentality”,²⁰⁴ others have phrased it as “corporate ego”²⁰⁵ reflected by the ego of the CEO of the companies or even “powerful person” or “power hungry”²⁰⁶. It is however clear that it is the actors in the alliances that are in the position to exercise power over other actors in the network through coordination or control of resources and activities.

In the network perspective power structure in some form is essential because activities and resources are, to some extent, organised through the bases of the power relation between actors in the network²⁰⁷. On the other hand power on the free market is viewed very negatively and transaction should be free from being influenced by power. Furthermore in the hierarchy or vertical integrated firm, power is much more accepted and is often used to centralise things such as decision making. Axelsson points out that analysing power in a dyadic relationship between companies is problematic and in an inter-organisational relationship, that includes more participants and more complicated structure, it gets increasingly difficult to make power explicit or understandable²⁰⁸. Despite some difficulties power is clearly closely connected with the inter-organisational relationship and its is necessary to include it in all analyses of such relationships.

²⁰³ Lorenzoni, G. & Baden-Fuller, C.

²⁰⁴ Lorange, P. & Roos, J., page 107.

²⁰⁵ Pfeffer, J., page 109.

²⁰⁶ Leavitt, J H. & Bahrani, H., page 121.

²⁰⁷ Hakansson, H. & Johanson, J.; Axelsson, B.

²⁰⁸ Axelsson, B.

V.4.2.4 Uniqueness of SMEs

It can be argued that small and medium size companies do not have as many internal organisational barriers as larger companies due to much fewer layers in the hierarchy and departments. On the other hand the “softer” part, such as culture and attitude could easily build barriers towards an interacting relationship. Paradoxically, the issues that facilitate the motivation for SMEs to take part in strategic alliances can also work as barriers to successful participation of the company. These issues arise from a lack of resources, such as money, knowledge and time. It is difficult to generalise about the difference between the structure of small and large companies.

However the author attempted to do so in Table V.7 with the warning that this difference varies between companies.

Difference between large and small companies		
Factor	Large companies	Small Companies
Organisation	Formal hierarchy and bureaucracy	Lean and informal
Culture (company)	Based on formality and status inside the companies	Based on entrepreneurial characteristics
Decisions	Slow, have to go between many levels and are finally made in the top level	Fast and done at the workplace
Management	Traditional mechanism management	Leadership, built on spontaneous responses
Changes	Slow and use the scale of size	Fast and build on innovation
Management of partnership	Middle managers that often do not have the authority to make necessary decisions	Top managers that have all the authority to make necessary decisions fast.

Table V.7 Differences between large and small companies

Yves L. Doz found out, in his research on partnerships between large and small companies in the technology industry, that the odds are against such partnerships, and most fail to meet the objectives of the partners. What is interesting in his conclusion is that the attitude of managers and owners of the small companies is characterised by a fear of being taken over by their large partner²⁰⁹. This could suggest that managers in SMEs could build up a negative attitude and culture due to the fear that another company will overtake their core resource that is often knowledge.

²⁰⁹ Doz, L. Y.

V.5 Conclusions

What emerged from the literature review is that there is a clear difference in emphasis between the newly emerging network perspective and the more traditional dominant perspectives, such as the transactional cost theory and competitive analysis of Porter. It is the author's conclusion that it is necessary in researching strategic alliances to view the participating companies as a part of the network and embedded in the environment that it is working in, but not as a single free standing unit. At the same time, it is necessary to recognise that the environment of a company, whether it is participating in strategic alliances or not, is a mixture of cooperation and competition. In this environment a company needs to be able to cooperate as well as compete and even be able to do so with the same company²¹⁰. The network perspective is also a very useful guide in studying strategic alliances where strategic alliances can be seen as a part of the bigger network in which the company is participating. It is clear though, in the author's mind, that strategic alliance is a narrower concept than the network concept. Hellegren and Stjernberg define the concept "network" as a "*group of organisations that are related to each other, but have no common hierarchical structure of responsibility and only vague criteria for judging who is part of the network*"²¹¹. On the other hand strategic alliance is defined here as *where two or more companies cooperate together to attain shared strategic objectives*. This definition should make it clear that companies participating in strategic alliances need to have shared objectives in terms of what they are going to achieve from their participation in the alliance, which narrows the scope of the alliances from what is known in the network perspective.

It is concluded here that the network perspective and increased emphasis on cooperation has introduced new dimensions in the discussion about the organisational form (hierarchy and market) of firms. Ouchi put forward an interesting view where he splits the market and hierarchy into four parts and brings in the option of having a win-win strategy instead of just a win-lose

²¹⁰ Contractor, J. F. & Lorange, P.

²¹¹ Hellegren, B. & Stjernberg, T., page 89.

strategy that is dominant in the two other forms²¹². Hence, cooperation or networking should be seen as the third option to the hierarchy and market. It is necessary though to recognise that in the “real world” more mixtures of forms exist and the boundaries between forms are not as clear-cut as many academics would like them to be.

In many cases the discussion about the governance of the network and strategic alliances moves between the extremes of network and hierarchy. On the one hand there is an almost grassroots emphasis on the network perspective, where the governance is based on mutual adjustment and learning; on the other hand there is the very hierarchical style of governance, which is known in many joint ventures where one parent dominates and is responsible for the management aspects of the child²¹³. What becomes apparent from most of the literature on governance of companies' relationships is the need for coordination. In most cases coordination is achieved through a mixture of formal and informal administration mechanisms, which in many cases can be problematic due to interdependency of each company in the alliance. Due to this interdependency some element of opportunism will always be included in the transaction in the alliances. Each company has the option of comparing the transaction inside the network to the free market or vertically integrated firm. For SMEs this comparison may be different from what is known in the literature of large companies. SMEs have often limited opportunities for vertical integration due to limited resources; transactions on the free market can limit their opportunities. Hence the SMEs often face co-operating in one way or other, not through choice, but rather through the necessity of having to operate in the international market today.

From the SMEs point of view, one of the most interesting elements that has emerged from the literature review is the discussion about the need for some leading companies to be responsible for the coordination to some extent and, more importantly, to be the strategic leader in the alliances. The strategic leader, or what Lorenzoni and Baden-Fuller calls the “strategic

²¹² Jarillo, C. J.

²¹³ Badaracco, J. L. Jr.

centre”, is in many ways in contradiction with the grassroots movement in the network perspective. However, upon closer examination of the role of the strategic centre it becomes clear that it is not meant to operate as a centralised headquarters in a multi-business company. Rather it is meant to be encouraging and to create an environment where other companies can operate and exercise innovation and creativity. In this environment the mutual adjustment and flexibility that is emphasised in the network perspective can then flourish even better than if no single company has the role of leading the alliances. Lorenzoni and Baden-Fuller point out that lack of strategic leadership is one of the key weaknesses in the management of strategic alliances. In the same way it can be said that in the network perspective, the lack of clarity and of a better understanding about the governance of networks are some of the main weaknesses in that perspective. It can be suggested that for SMEs working in an alliance the need for strategic leadership is even more important, due to lack of resources and limited size often making them unable to put much effort into forming a shared strategy or vision.

Strategic leadership and central firms bring in certain issues of centralisation and formal structure to the governance of strategic alliances. Clearly a company that is in the centre of an alliance, as well as participating companies, are highly dependent on making the position of the central firm powerful, this may tempt the central firm to make their piece of the cake bigger than it would be otherwise. This can be dangerous in marketing alliances where the connection to the market and ownership of brand is of great importance. A central firm having such a position is in a powerful position against other participating firms. Also the strategic leadership raises the question of the importance of strategy, shared objectives and vision to the governance of the alliances. Is it, for example, possible that shared strategy could guide participating companies more efficiently than using more formal methods of authority, and could reduce the need for formal methods of coordination in the alliance. For alliances with a high number of participating companies, the strategic leadership and centre imply that it could be an effective way of co-ordinating resources and activities

which otherwise could be difficult. For such alliances it is essential to have strategy and structure, so that all the participating companies can work within it and benefit from it²¹⁴.

This literature review has also shown that there are many influencing factors on the governance of strategic alliances. These factors include for example, the nature of the alliance, the number of participating companies, interdependency between companies in the alliances and the dependency of companies on the alliances. Other factors include, for example, the internal barriers that are in many companies towards inter-organisational relationship. These internal barriers are, for example, willingness to co-operate, attitude, trust, culture and the organisational structure. Other elements that influence the strategic alliances are, for example, power structure in the alliance, and the balance of power between participating companies. All these elements and more influence the way the inter-organisational relationship is managed which is in most cases through a mixture of informal and formal administrative mechanisms.

The understanding and discussion of the administrative coordination in strategic alliances is far from clear in the academic literature and it has been pointed out that further research is needed in that field. Recommendations for further research taken from Osborn and Hagedoorn include a *“clear need for more studies concerned with how alliances are actually established, who manages various aspects of their operation, and how managerial lateral and quasi-lateral relationships across legal entities differs from managing more hierarchically structured entities”*²¹⁵. In a similar way Axelsson suggests *“more research is required into the long term development of such alliances and methods of management to support a better understanding of the way they operate”*²¹⁶. Alter and Hage add that there is a need for further research on the operational level of companies' relationships which depends much more on the informal co-ordination mechanisms because this is the critical point in the relationship where the problems of mismanagement can

²¹⁴ Nam, H. S.

²¹⁵ Osborn, N. R. & Hagedoorn, J., page 267.

²¹⁶ Axelsson, B., page 247.

occur²¹⁷. From these quotations it is clear that further research is needed into the operations of strategic alliances.

The empirical research of the two marketing companies in the Icelandic fish industry (see Chapter VI and VII) is meant to contribute to these identified gaps in the literature. The main object of this research is to analyse key factors in the role of the “central firm” in strategic alliances between large groups of SMEs. The aim is to increase understanding about this development and generate knowledge emerging from the empirical part of the study. Concerning this research the most relevant elements emerging from the literature review are the need for strategic leadership and the administrative structure in alliances. These are mainly due to the high number of participating companies and the nature of the alliances (that is, spanning over many levels of the value adding chain with the marketing companies in the centre, leaving them in the position of central firm). It has emerged from the literature review that there is no clear formula or model to study strategic alliances. The network perspective offers helpful guidance but, as has been pointed out, further research is needed to establish a better understanding of inter-organisational relationships. The use of the network perspective affects this research because it is not enough to study the two marketing companies as a single unit but instead it is necessary to look at the whole process from the processing companies to the customers. In order to do that the following topics that have emerged both from the literature review and Chapter IV about the Icelandic fish industry will be studied:

- 1) The role of the two marketing companies as “central firm” in alliances spanning over several levels in the value adding chain
 - What is included in the role?
 - How do participating companies view the role of the central firm?
 - What dangers are involved in the role of the central firm?
- 2) The role of the central firm in the “governance” of the alliances as a whole and what impact changes have on the administrative mechanism of the alliances.
 - Through what mechanism are the alliances co-ordinated?
 - How has this mechanism changed?
 - What has influenced these changes?
 - What is the importance of strategy in the administrative mechanism?

²¹⁷ Alter, C. & Hage, J.

- 3) The structure of the strategic alliances and how these have evolved and developed.
 - Draw out the different forms that the alliances have taken through the operation time
 - What has influenced the structure?
 - What characterises the structure?
- 4) Finally, the academic literature in strategic alliances will be compared with the findings of this research.

Topic one includes studying the general role of the marketing companies as “central firm” in the alliances and how participants view that role today; changes in that role will also be studied. Topic two is more specific about the role of the central firm in the governance and the administrative mechanism of the alliances. This topic also includes what methods have been used to co-ordinate activities and actors in the alliances and how that has changed according to changes in the role of the central firm. Topic three includes analysing the main elements of the structure and different form that the alliances have taken over the operation time, but not the economical justification of the structure. Analysing the main structural form that the alliances have taken, as well as their characteristics, is considered to be essential in order to get a more holistic picture of the role of the central firm in the alliances.

VI Research Findings

In this chapter the two cases, Union of Icelandic Fish Producers and Icelandic freezing plants, are presented. The discussion of each case is split into three parts. First the historical development of the companies is introduced which is mainly built upon archival data, although some interviews were taken to clarify some aspect of the history and to be able to go deeper into some matters. The second part includes more analysis concerning the research aims, that is, the governance of the network and the role of the marketing companies as a central firm in those networks. This part is based on interviews as well as archival data. In the last part the conclusion from each case is put forward.

VI.1 Union of Icelandic Fish Producers

Union of Icelandic Fish Producers Ltd., abbreviated UIFP, was established in July 1932 after the merger of three of the five salt fish merchants and pressure from the commercial banks and government. In addition to this, producers and ship owners in Iceland supported the establishment of UIFP. The main objectives were to improve the organisation of the export of salted fish from Iceland and minimise internal competition in the market. This was achieved by UIFP taking care of the sales (for a commission) for the producer. If exporters and producers had not reacted in this way it seems clear that one of the options they were facing was the establishment of a state owned company that would have a monopoly on all sale of salted fish from Iceland¹. UIFP was initially only meant to be a temporary solution but, after an experimental year, the government granted UIFP a virtual monopoly on the export of salted fish.

VI.1.1 History and Development

The operation of UIFP can be divided into four periods. The first period is from the establishment in 1932 to 1957 when UIFP went through difficulties leading to changes in operation. The second period is from 1957 to 1990

¹ Valdimarsson, U. V. & Bjarnason, H.

when the operation was characterised by monopoly of export and taking care of matters of interest for the producers. The third period is from 1990 - 1993 when UIFP faced increased competition in exporting leading to changes of ownership of UIFP. The last period is from 1993 until the present, when UIFP has operated as a limited liability company.

VI.1.1.1 Establishment and Entrepreneurship 1932 - 1957

UIFP was established as a non-profit², co-operative company whose main aim was to sell its members' products for as high a price as possible and to push for increased quality of production³. The aim of the company was not to build up assets but to retain sufficient commission to enable it to pay the operational costs. Then, at the end of each year, the amount left over after the operational cost had been paid was given back the members in proportion to their export through UIFP.

During the first three years of UIFP, it operated in the form of a merger of three exporters' and producers' companies in Iceland, where the managers of these three companies acted as managers over UIFP. Due to the changes of UIFP in May 1935, the nature of the company changed to become a joint venture of nearly all salt fish producers in Iceland, where the producers were the "parents" (owners) and UIFP was the "child"⁴. To get the necessary acceptance of the government of Iceland and the exclusive export licence, representatives of companies that accounted for at least 65% of the total production of salt fish in 1934 had to be willing to join this joint venture. UIFP got the support of almost 66% of the producers, leading to agreement of the establishment of this joint venture of salt fish producers⁵.

When UIFP was established, there were around 322 members, but after a difficult period during WW2, in 1949 the number of members was down to around 138; mainly due to there being fewer companies in salt fish

² The term "non-profit" is used here in the sense that UIFP was supposed to make profit but to return it to members after operational and other costs and investments had been paid for.

³ Valdimarsson, U. V. & Bjarnason, H.

⁴ See, for example, Harrigan, R. K., 1985 for a definition of joint venture.

⁵ Valdimarsson, U. V. & Bjarnason, H.

production, as well as competition from other production methods such as freezing⁶.

Another aspect of the changes in 1935 was to give UIFP stronger financial status, and in order to do so a reserve fund was established that was 0.25% of the total sales value of the exported fish. This fund was connected to each member's contribution and therefore each member of UIFP owned a separate slice of it, which they could get paid back in 10 -12 years, according to agreements with UIFP, if they decided to leave the organisation. Due to the fact that UIFP returned its profit to the members it meant that UIFP, as well as IFPC, was free from paying taxes in Iceland.

Operation of UIFP was based on commission sale of the members' product, which was coordinated from an office in Reykjavik that took care of the sale through representatives located in each of the main market countries. Other operations during this time included the arrangement of transport of the products as well as supplies of accessories for the production of salt fish. During the period from the end of WW2 to around 1965 there were around 8-10 representatives, two were Icelandic and the rest were foreigners with business connections in the market⁷. In addition to this representative system, managers, the chairman of the board or other members of the board went on regular sales trips abroad.

UIFP started its operation in troublesome times for export of salted fish due to overproduction of salted fish worldwide followed by the civil war in Spain in 1936, which closed the single most important market for salted fish. Soon after that, WW2 started and again the markets for salted fish collapsed. In addition to this, other production methods such as freezing, took over as the main production methods for fish in Iceland. It was not until after WW2 that UIFP could start its operation again after having almost stopped during the war. Before WW2, 10 - 15 people worked in UIFP but during the war, in 1943, UIFP had only three full-time employees working in the sales office: an office manager, an accountant and a secretary

⁶ Valdimarsson, U. V. & Bjarnason, H. The precision of these figures is debatable due to different methods in counting members over the years.

⁷ Valdimarsson, U. V. & Bjarnason, H.

(other jobs such as managerial ones were part time). After WW2 the operation increased, as did the number of staff, and in the 1950s 10-15 people were employed by UIFP⁸. Other operations of UIFP were a canning plant, which UIFP included during the period 1938 - 1952⁹. This plant was supposed to be an experimental plant for the canning industry in Iceland. In 1952, the plant was sold because UIFP found it had delivered its objectives and that the plant did not fit into its operation. UIFP planned to use the money from the plant in connection with plans to buy a cargo ship, but this did not eventually happen at this time.

From the establishment of UIFP in 1932 to 1935 the board had five members, two nominated by the banks and three from the exporters that merged with the establishment of UIFP. During 1934 and the first part of 1935 producers become increasingly dissatisfied with their influence in the running of the organisation, especially producers from the rural areas of Iceland whose opinion was that they did not sit at the same table as producers closer to the headquarters in Reykjavík. This dissatisfaction led to changes of UIFP's governance, which were agreed during an annual meeting in May 1935. After the previously discussed changes of UIFP in May 1935, the number of members of the board was increased to seven, where the Icelandic government nominated two, three came from producers and two from the two banks, Landsbankinn and Útvegsbankinn. In 1938, Útvegsbankinn stopped nominating its member of the board and that seat went to the producers, but Landsbankinn kept its member until 1976.

From May 1935, the voting system on the annual meetings was such that each member got a vote, which was proportional to the quantity of merchandise that the particular company sold through UIFP. No company, however, could have more than 8% of the total votes, in order to avoid having one single company with too much power or influence on UIFP. This was done to meet the demands from political parties and the Federation of co-operative companies (SÍS) that sold through UIFP, which put great

⁸ Valdimarsson, U. V. & Bjarnason, H.

⁹ This canning plant was operated separated from the sales operation of UIFP and is not included in the number of employees of UIFP.

emphasis on equality of the members. This equality and limitation of power of each company was in opposition to what a membership meeting in May 1935, had agreed, where they argued that votes should be in proportion to products sold through UIFP¹⁰.

In 1943/44, the formal nomination of the two representatives from the government ran out. However, according to proceedings of UIFP boards they both attended meetings of the board until November 1944 when one of the representatives stopped attending, and the other one continued until November 1946¹¹. After that, until 1952, the board had only five members but in 1952 the number increased again to seven where the producers got the two extra seats. Producers had a majority in the board from 1938 when the seat of Útvegsbankinn went to the producers, then after the increase in the board in 1952 the producers had six members and Landsbankinn one.

During this period there were two to three managers of UIFP. In the first years of UIFP operation there were three that is, the former managers of the three exporting companies that established UIFP. After 1947, two managers controlled UIFP's daily operation.

VI.1.1.2 Monopoly 1957 - 1990

The period 1957 - 59 was in many ways an important turning point in the history of UIFP due to members' increasing dissatisfaction with its operation. There were mainly three issues which dissatisfied the members. Firstly, the sales organisation in many ways appeared to have stagnated; secondly, the members' found that UIFP did not pay as much attention to matters of its members common interest as it should have done; thirdly, the members were of the opinion that they had very little to say in the governance of UIFP as they found the board too remote from the members and their needs. A reflection of this criticism was apparent in the composition of the board, where in 1959 not all of the board members were

¹⁰ Valdimarsson, U. V. & Bjarnason, H.

¹¹ Valdimarsson, U. V. & Bjarnason, H.

in direct contact with salt fish production, and most of them were getting rather old and had been on the board for a long time¹².

The dissatisfaction with the governance and the increased emphasis on matters of common interest are closely connected. It was not until after a meeting of at least 39 members of UIFP in September 1959, where they planned to establish an organisation separate from UIFP to take care of common interest matters of salt fish producers, that the board of UIFP started to react to the members' requests to act more in such matters. This resulted in UIFP establishing a special interest committee to take care of common interest matters with three members nominated by the board and six by the producers¹³. By this UIFP widened its aims and acted increasingly as a pressure group in common interest matters such as putting pressure on the government about better operation bases for salt fish production, on banks about increased loans towards producers, on the governments fund controllers about increased loans for new equipment and houses, and other matters that could concern the salt fish production¹⁴. This emphasis on common interest matters is easily understandable considering that the economy in Iceland during this time was under great interference from the government. This meant that having a strong position in putting pressure on government was very important and in many ways essential in order to have operational bases for the companies.

The dissatisfaction of members lead to the members becoming much more active in the governance of UIFP, first through the common interest committee and secondly by changes on the board where more active producers came into the board in 1960 and then in 1965 when all the seven substitutes started attending all board meetings. Later, in 1983, the number of the board members was increased to fourteen and the substitutes were promoted to full members.

It can be argued that around this time (1960) the strategy of UIFP changed in that it stopped acting only as a sales organisation and took up much

¹² Valdimarsson, U. V. & Bjarnason, H.

¹³ Valdimarsson, U. V. & Bjarnason, H.

¹⁴ Valdimarsson, U. V. & Bjarnason, H.

broader service with its members as the interest matters reflect. The major players in this change were clearly the producers that found UIFP to have stagnated. It could be questioned whether the protected environment that followed the exclusive licences, and having a virtual monopoly of export, made the environment of UIFP too secure and lacking of the motivation that often comes with competition.

Changes in the sales system came around the middle of the 1960s when increased emphasis was placed on sales trips of managers and the chairman. In the same time, less emphasis was placed on the representative system, which meant that their number declined, as well as their commission. UIFP also opened its first sales office in Italy in 1965, which operated there until 1989. By establishing a sales office, UIFP was aiming to build up a closer relationship with the customers as well as cut the cost of the sales system. The sales system was always under close inspection by the members; for example, they compared it to the sale systems of IFPC and SÍS, which were also built on sales offices abroad. However, the representative form by UIFP was kept more or less unchanged until 1987, when UIFP opened a sales office in Barcelona in Spain that in 1990 became a subsidiary, Union Islandia, which was the first subsidiary that UIFP established abroad. In addition to the sales operation there, the subsidiary operated cold storages and took care of distribution of the product to customers¹⁵.

Another change on UIFP's operation that is worth mentioning is that, around 1980, UIFP started to take loans to be able to offer its members quicker payment for their production and save some costs in credit that was secured by inventory. In this way UIFP used the economy of size and got more effective loans than individual companies could get, and this cut the financial cost for the producers.

During the period 1957 - 1990, the operation of UIFP increased very fast mainly due to increased service to members as well as the broadening of its role. An example of this increased service with members and operation of UIFP occurred in 1962, when UIFP hired employees to take care of

¹⁵ Valdimarsson, U. V. & Bjarnason, H.

technical matters for both UIFP and its members. This was the start of the operation of a technical department of UIFP¹⁶. In 1967 UIFP built its own warehouse where fish were collected before being exported, and could also be packed and graded if necessary. In 1972, UIFP hired an employee to take care of the quality control of the products of its members, which was the birth of a quality department. Later, in 1984, UIFP started its own R&D work to develop new products. Following the establishment of the R&D department, UIFP operated the packing of fish in consumers' packing from 1987 to 1990 when the equipment was passed over to producers in Iceland¹⁷. Other changes that followed the increased operation of UIFP were all kinds of information sharing with members, in the form of production guides, guides to expected price and stocking time, as well as regular newsletters. During this time, the number of employees rose from 10 -15 in the 1950s and 60s, to just over forty in 1990. Around 25 employees were working in the headquarters in sales and administration and the rest in quality control, R&D, warehouses and other handling of the production.

The number of members fluctuated over this period but in 1970 there were 219, 311 in 1982 and in 1986-'87 it reached its peak when the number rose to 405, but in 1991 the number had gone down to 286¹⁸. Most of these members are very small companies with production under 25 tons.

From 1962 - 1978, there was only one manager of UIFP and then two were titled as managers until 1985 when one of them retired. In 1986, the acting manager, Friðrik Pálsson, was hired as the manager of IFPC and after that, Magnús Gunnarsson was hired as the manager until the change of ownership of UIFP in 1993. Most of the time when two or more managers were acting in UIFP they took care of different market areas, and office managers were responsible for the day-to-day operation of the office and domestic operation. From 1986 until 1993 the manager acted more as a spokesman for UIFP and its members, aiming at improving the competitive

¹⁶ Valdimarsson, U. V. & Bjarnason, H.

¹⁷ Valdimarsson, U. V. & Bjarnason, H.

¹⁸ Valdimarsson, U. V. & Bjarnason, H.

status of salt fish producers. In the same time, a new job of assistant manager was created which the acting office manager took over. The main activities of an assistant manager were to take care of all sales operations of UIFP¹⁹.

VI.1.1.3 Increased competition 1990 - 1993

During the period before 1990, UIFP almost had a monopoly on the export of salted fish due to limits in the number of export licences granted by the ministry of Fishery and later the Foreign Ministry. However, this time other companies got a limited licence to export salted fish from Iceland, but usually in very little quantity or by rather strict conditions. Different pressures were put on these export licences, for example in 1987 when producers not bound to UIFP started exporting fresh split fish²⁰ to Denmark or the UK where it was salted and then sold on to Spain, mainly as Icelandic salted fish. This meant that the exporters could circumvent the export licence that blocked them from exporting fully produced salted fish from Iceland as well as circumvent the high import taxes into the EU. Other pressures during this time came from the imminent implementation of an international contract between EFTA and the EU about the European Economic Area and the single market, where Iceland had to adapt to free trade between European countries. To cut a long story short, in 1991, Iceland's Foreign Ministry granted companies other than UIFP limited licences to export salted fish mainly to Latin-American countries. The Foreign Ministry also granted other companies experimental licences to sell salted fillets to Mediterranean countries, and, in 1992, to sell split fish²¹. After these experimental licences were granted in 1991 and 1992, and with the prospect of free trade with EU countries, it was clear that the exclusive licences that UIFP had on export would be abolished; they were indeed abolished in January 1993.

¹⁹ Valdimarsson, U. V. & Bjarnason, H.

²⁰ Split fish is fish that has been split open and the front part of the spine removed.

²¹ Morgunblaðið 27/3 '94, interview with Jón Ásbjörnsson.

In 1990, UIFP clearly changed its strategy when it bought a French company Nord Morue, that operated secondary processing and selling of fish products. The main emphasis of this company was on producing consumer packed products from salted and smoked fish. With this UIFP was aiming to avoid high import taxes on fish products in the EU, get a broader knowledge of the production of different fish products, gain important business connections and be more flexible in order to respond more quickly to the increasingly fast rate of change of the food market²². In many ways this can be seen as a continuity of its experiment with the packing centre in Reykjavík, but there was a clear change in strategy because UIFP had not been involved in direct processing before. The involvement of UIFP in secondary processing in France means that UIFP is going deeper into the supply chain by increasingly selling products to supermarkets instead of rather traditional salt fish markets in Mediterranean countries. Hence, the market for UIFP is changing from small shops and distribution companies for salted fish to direct selling to supermarkets where reliability and long-term relationship is often one of the main issues²³. Following the operation of the Nord Morue, UIFP's strategy in sales organisations started to change. Before 1990 almost all of UIFP's sales were commission sale of its members' products, but after 1990 UIFP increasingly bought the fish from producers instead.

Before 1990, UIFP depended completely on the Icelandic producers for fish to sell, and the producers also depended on UIFP for selling their products. With the acquisition of the company in France, UIFP started to become more independent from its members because the secondary plant bought raw material from more than just Icelandic producers.

Another aspect of the strategy changes during 1990 was that members started serious discussions about changing the form of the organisation, realising that the organisation was not very fit for free competition, mainly due to its laws and duties with its members. These duties concerned information sharing, equality of members inside UIFP, having to act as an

²² Based on interview with former manager of UIPF and Valdimarsson, U. V. & Bjarnason, H.

²³ Cook, R.; Fearn, A. & Dedman, S.; Wysocki, F.A.

interest group and other services with the members that were not compatible with free competition. The laws of UIFP made it in many ways inflexible and very dependent on its members, especially in financial matters. An example of this is that UIFP had to return the profit to members and therefore depended on them to agree on leaving more of the profit in the company when it was needed for some investments. Due to often-poor profitability of the producers, this could be difficult and then UIFP had no other option than to get the necessary funding as a loan. This could have delayed changes and was not a feasible form for free competition. Hence, the next step to increase UIFP's ability to become more competitive was to grant it more freedom and independence from the producers. In order to do that it was necessary to move from the duties and the equality principle that had been the essence of connecting UIFP with its producers. An annual meeting for 1991 agreed on changes aiming at giving UIFP more flexibility and independence from its members. The suggestion for changes took on the following issues, among others:²⁴

- Grant UIFP more authority to influence the quantity and production of producers.
- Grant UIFP authority to let individual producers take on special production that is not necessarily on offer to all producers.
- Grant UIFP more freedom in ways of payment to producers to be able to return higher prices to the producers
- Grant UIFP permission to buy products under its own name as well as grant permission to own and operate primary processing companies, both domestic and foreign, if they were appropriate to the operation of UIFP.
- Grant UIFP permission to sell all products those members wanted not just salted fish.
- Grant UIFP permission to sell for non-members' companies.

These changes, which came were finally implemented in 1991, did not go too smoothly through the system of UIFP; for example, the manager, Magnús Gunnarsson, resigned after a members meeting in October 1990 had failed to agree whether to stop exporting fresh split fish in competition with their own salt fish sold through UIFP. Later the same month the

²⁴ Valdimarsson, U. V. & Bjarnason, H.

manager withdrew his resignation when over 90% of the members signed a statement of support for him²⁵.

At the same time as UIFP faced this increased competition, the fish quotas were declining, leading to a decline in salt fish production. This meant that UIFP's operation declined and from October 1992 to October 1993 the number of staff was cut to half of what it had been (from just under 50 to around 25)²⁶. This also affected the profitability of UIFP; in 1990, UIFP made around 483 million ISK. (Icelandic króna) in profit, and in 1991 it made a profit of 150 million ISK., but in 1992 it made a loss of 118 million ISK., which was the first time in the history of UIFP that it had not returned a profit on its operation.

Due to these difficulties, a members' meeting on 26th of January 1993 agreed that it was necessary to go one step further in the changes of UIFP by changing the ownership of UIFP into a limited liability form, to increase the flexibility of UIFP as a company. In order to achieve this, UIFP was abolished and a new company, UIFP Ltd., was established in February 1993. The allocation of shares in the company was in proportion of the members' ownership in the reserved fund, and present or former producers owned almost all of the shares.

In 1993, UIFP sold products for around 200 Icelandic companies, where 50 (i.e. a quarter of the total number of companies) produced 86% of the total quantity of good. The other 150 companies produced only 14% of the total quantity of UIFP's sale in 1993²⁷.

The motivation for the changes of UIFP during this time seem to have come from outside pressure, mainly from other companies, politics and the implementation of international contracts which created pressure for the abolition of UIFP's exclusive licence. Internal motivation does not seem to have greatly influenced the changes of UIFP, neither from the managers nor from the members. In many cases it seems clear that managers and

²⁵ Morgunblaðið 24/11 '90.

²⁶ Morgunblaðið 26/11 '93 interview with Magnús Gunnarsson CEO of UIFP.

²⁷ Morgunblaðið 12/5 '94.

members of UIFP focused more on preserving the exclusive licence rather than adapting to the changes of their environment in time. However, both UIFP and its members had in many cases good reasons for supporting changes in UIFP. These reasons, included, for example;

for UIFP

- more flexibility by working as a limited liability company
- better access to money through increased share
- more expansion possibilities by selling for non-members
- more emphasis on business matters instead of common interest matters

for members

- exit barriers for leaving UIFP would become lower
- better value for their share in UIFP
- more options in selling their products

These exit barriers for members to leave UIFP included, for example, the ownership in the equity fund of UIFP, which was paid out over a long time if members decided to leave UIFP. In addition to that, it is clear that the value that members got from the equity fund was far from what the market price for the share in UIFP would be if it were a limited liability company. This could have increased the pressure for the ownership change of UIFP, especially considering the poor financial status of many companies inside UIFP²⁸.

VI.1.1.4 Transformation 1993 - 1998

UIFP Ltd. took over equity and operation of UIFP on 11th of October 1993 when the accounts of the old UIFP had been settled. After the establishment of UIFP Ltd., around 700 shareholders owned the new company, where most of them were present or former fish producers. The biggest owner had a 4.71% share so the ownership was well distributed and no one had obvious power to dominate the company. In March 1997, UIFP was registered at the Icelandic Stock Exchange market, meaning that its shares

²⁸ See for example discussion about Icelandic fish industry in chapter III.

were on the free open market, and that UIFP had to give information on a regular basis concerning its operation and profitability²⁹.

In the year of 1993/94 the company hired a new general manager Gunnar Örn Kristjánsson after the former manager had resigned, in order to give the board and the new manager a clean table to decide a new strategy and vision³⁰. Apart from the change of manager, the staff of UIFP was the same as before the ownership change.

Although this ownership change did not formally change the operation of UIFP as a company, it is evident that when UIFP was changed into a limited liability form and having a new general manager, the strategy of the company changed dramatically. The main changes that followed were that UIFP had much more independence from the producers in Iceland and did not only act as a sales organisation for the Icelandic processing companies. Instead UIFP started, for example, to buy and sell salt fish from foreign producers, beginning in Norway. This move led to the establishment of a subsidiary in Norway, UIFP Union a.s., in 1995, which was later changed into Mar-Nor a.s., to take care of selling products from Norwegian companies. UIFP also started to buy the fish from the producers instead of selling it in commission sale, which meant that producers got paid earlier, but at the same time meant that there was often the opportunity for UIFP to buy fish when the price was low and keep it until the price went up before selling it again³¹.

In 1994, UIFP established a company in Spain, Copesco & Sefrisa s.a., with one of the biggest Spanish salted fish distribution companies. This company took over the operation of UIFP's subsidiary in Spain, and was intended to strengthen UIFP's position on the market. In 1996 this cooperation between UIFP and the Spanish partners collapsed, leading to the resurrection of UIFP's subsidiary in Spain to take care of UIFP's activities there. In 1996, UIFP went into a new sector by buying a 40%

²⁹ UIFP Annual Report 1996.

³⁰ Morgunblaðið 26/11 '93 interview with Magnús Gunnarsson CEO of UIFP.

³¹ Morgunblaðið 21/5 '95 interview with Gunnar Örn Kristjánsson CEO of UIFP.

share in Icebrit Ltd., which is based in Hull, UK and takes care of selling fresh fish.

The expansion of UIFP boomed in 1997, starting in March when UIFP bought the Hvítanes, a cargo ship which previously had taken care of about 80% of the transport for UIFP from Iceland and Norway to France and Mediterranean countries³². In May, UIFP bought a 50% share in a Norwegian processing company to strengthen its position on the Norwegian market. Then in September 1997, UIFP bought two Canadian companies in Nova Scotia: Sana Souci Seafood Ltd., which operated fish processing, secondary processing, distribution and marketing of salt fish mainly in North and South-America; and Tara Nova Ltd., which is primary a processing company³³. This meant that UIFP bought access to the fish market of (mostly North) America, where it had not been strong before. The final move of UIFP in this foreign investment was in November 1997 when along with its Norwegian partners, it bought another primary processing company in Norway.

After these changes, it is estimated that UIFP and subsidiaries controlled around 16% of the total salt fish sale in the world, making UIFP the biggest single seller of salted fish in the world³⁴. In table VI.1 a few essential figures of the financial status of UIFP are summarised. It can be seen that the operation has expanded quite rapidly, its revenue has increased by around 25.5% from 1993 to 1996. In addition to this the latest investment in 1997 is estimated to have boosted the revenue significantly, by about 1.8 billion ISK or 17.5% compared to revenue in 1996. Profitability, however, has been moderate from 3.6% of operating revenue in 1994 to 1.1 % in 1996, compared to the general nominal interest rate on non-index secured loans in Iceland during that time falling from 14.4% in 1993 to 12.4% in 1996³⁵.

³² Morgunblaðið 9/4 '97.

³³ Morgunblaðið 12/9 '97.

³⁴ Morgunblaðið 12/9 '97.

³⁵ Seðlabanki Íslands, Hagtölur mánaðarins ágúst, 1997.

Year	Operating revenue in ISK '000	Return on operation revenue	Equity ratio	Return on equity	Number of staff	
					Icel.	Abroad
1993	8,209,000	1.8%	25.4%	10.3%	N/A	N/A
1994	9,200,054	3.6%	21.2%	24.1%	N/A	N/A
1995	9,473,7333	1.8%	18.9%	20.5%	59	162
1996	10,304,499	1.1%	25.4%	9.0% ³⁶	70	154
1997	11,675,880	1.3%	24%	11.0%	64	330
1998	18,834,193	2.7%	28%	24%	60-70	776-786

Table VI.1 Consolidated financial key figures³⁷.

In 1999 came another boom in the growth of UIFP. In the beginning of the year (or from 1st of December, 1998) Íslandssíld hf., formally Icelandic Herring Board, merged to UIFP³⁸. Then in the autumn 1999, Icelandic Seafood and UIFP merged under the name of UIFP³⁹. In this way, UIFP diversified its operation significantly from the time before the merger with Icelandic Seafood, when it defined its role as an “*international marketing and production company in chilled fish production*”⁴⁰. Now UIFP handles frozen fish products as well, so theoretically speaking it covers almost all forms of fish product exported from Iceland. Íslandssíld hf. was mainly in the business of marketing slated herring, which is not very different from UIFP’s business. Additionally, most of the biggest producers of slated herring are also big producers of slated cod and were already in business with UIFP. Hence the merger with Íslandssíld hf. did not signify a strategic change in UIFP’s operation. On the other hand the merger with Icelandic Seafood was different because the producers were in many cases bigger and the value adding is more than in salt fish production. This could create pressure on UIFP’s strategy and on its relationship with producers. This research does not take in account the merger with Icelandic Seafood because it did not happen until after the data collection and analysis was done. However, further discussion about possible effects is discussed in the conclusion chapter. Before the merger with Icelandic Seafood, in June

³⁶ This decline in revenue on equity is due to increased of equity by new share sold in 1996.

³⁷ Annual report 1993, 1994, 1995, 1996, 1997 and 1998. In this table revenue is taken from the coalition of UIFP the mother company and subsidiaries.

³⁸ Morgunblaðið 30.12.98.

³⁹ Morgunblaðið 29.09.99.

⁴⁰ Taken from UIFP strategy on the www.sif.is.

1999, UIFP changed its structure to improve efficiency. UIFP Iceland was then established to take over the operation in Iceland and connection to producers in the same way as the old UIFP had done. The UIFP Mother Company was established to head all its subsidiaries in Iceland and abroad.

VI.1.2 Analysis of UIFP case

VI.1.2.1 Forms and nature of the alliance

It can be argued that the UIFP network has been in three basic forms during its operation time. The first was the first three years after the merger of three biggest fish export and production companies in Iceland formed it. After that, in 1935, UIFP became a joint venture between producers for the export of their production. The third form is from 1993 when UIFP became a Limited Liability Company and the alliances changed from being joint ventures between producers to individual alliances between UIFP and each producer.

During most of this time, the form of the alliances has not changed much. The interaction between actors in the alliances has been between producers and the central firm, that is the UIFP Mother Company. Before 1993 UIFP had few marketing subsidiaries, but although they were few, there was very limited direct connection between each producer and the subsidiaries. This can be traced to the homogeneity of the products. The main form of interaction is therefore as presented in figure VI.1 where the entire interaction is between UIFP MC and each producer.

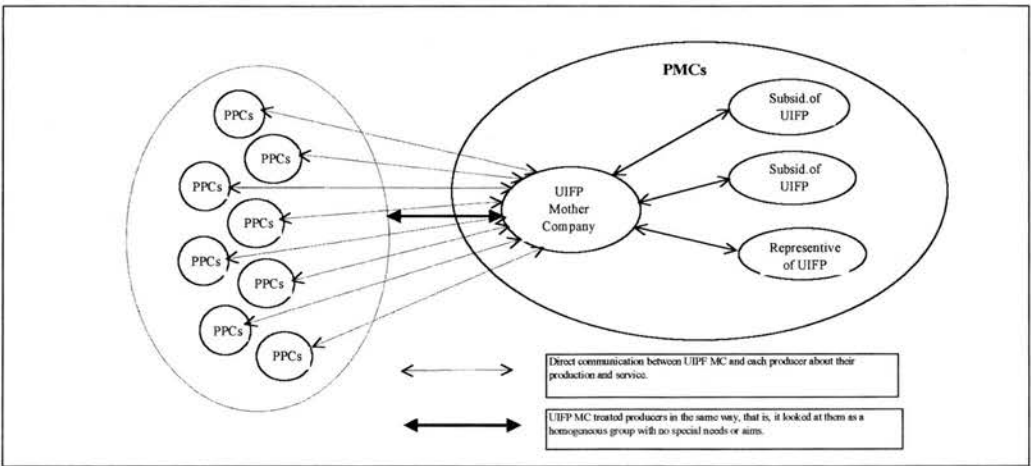


Figure VI.1 Main form of UIFP until 1993

During the time until 1993, UIFP treated producers on an equal basis. Hence, producers with different strategies to UIFP had difficulties fulfilling them due to the exclusive licences of export of salted fish from Iceland that UIFP was granted, almost exclusively, until 1993. Producers of salted fish were therefore enforced to sell their products through UIFP. Therefore, there was no freedom or real competition with other marketing companies for the producers. Not everyone appreciated this enforcement, as can be seen from the following quotation:

“It did not work out to produce carefully your products and bring it to markets when the sale organisation that sold it treated you as a dog. If I asked about something I was told that this was not for me to be concerned about.”⁴¹

This producer left UIFP in 1992 and established its own marketing company to sell its products. This enforcement meant that UIFP had to serve all producers no matter of how different the strategies and needs of the producers were. In the same way UIFP had, to serve big and small, good and bad as former manager of UIFP claimed.

“We had to serve all the producers no matter of the importance of the producers or the quality of its products. Often it took same time to serve producers that produced 600 ton and the small ones that produced 10 tons.”⁴²

Another factor that affected the alliances before 1990 was that the nature of the sale was very much influenced by international contracts such as the quota on toll free import to the EU countries. Much of the attention of managers of UIFP went into matters of mutual interest to the members and the role of UIFP was very much focussed on improving the competitive stance of salt fish producers and salt fish export, or as a former manager of UIFP claimed:

“The fish export from Iceland was in many cases not business to business relationship but rather contracts between countries as in former USSR as well in the Mediterranean countries. Selling to the Mediterranean countries turned out to be contracts with EU about the toll quota in competition with Norway. This called for putting pressure on officials in Brussels. In

⁴¹ Frjáls Verslun, interview with Sæunn Axels.

⁴² Interview with former manager of UIFP, I-32.

addition to this lot of energy went into the European Economic Area (EEA) contracts between 1988 – 1993 about the status of the fishing industry. This was very much on UIFP hands because there met both the companies blocks that is IFPC and IS."⁴³

With increased freedom in international trade, as well as increased freedom in the Icelandic economy, it was clear that there was increased pressure to abolish the exclusive licence of UIFP to export salted fish from Iceland. Other companies got limited licences to export salted fish from Iceland, leaving UIFP in the difficult position of having the duty to serve all producers while other companies got licences to export their products. As one employee of UIFP claimed:

*"The reason for UIFP difficulties when other companies were given licence to export salted fish was that there was an official system operated during this time which UIFP had to follow. We had to stock salted fish in the spring to sell in the autumn with the cost of stocking it. Then when other companies got free licence to bring in new product in the autumn without the cost of stocking them therefore in lower price it disorder the official system that was active. Therefore it was much better to give the export free instead of operating two systems where the competitive status of UIFP was limited having all the duties to producers."*⁴⁴

It is clear that the nature of the alliances until 1990 was just as much about acting as a mutual interest group as it was about being a sales organisation. After 1990, the importance of mutual interest matters declined, creating increased pressure to change the ownership form of UIFP. The difficult position of UIFP can be seen from the rather poor financial results after 1990, where in 1992 UIFP returned negative return on its operation for the first year in a long time. It was clear from the operation of UIFP that the form of a joint venture between producers, and UIFP's duties to producers, limited the effectiveness of its operation.

After 1993, the nature of the alliances changed from a joint venture to individual alliances between each producer and UIFP (see figure IV.2). In the first month after the ownership change, UIFP tried to make a contract

⁴³ Interview with former manager of UIFP, I-32.

⁴⁴ Interview with employee of UIFP, I- 25.

with each individual producer such that UIFP took on sales for producers on various different bases. As an employee of UIFP stated:

“In the beginning after the ownership change, we tried to establish contract with each producer. The idea was to have different groups of producers for example “A” group with producers that were committed to sell only through UIFP etc. We made this experiment but we found out soon that it was not worth all the bureaucracy that this demanded.”⁴⁵

UIFP still groups the producers into certain groups: the “A” group, comprising those producers that are selling their entire product to UIFP and get priority to sales and information; the “B” group that sells part of their products to UIFP and do not get the same priority to the information and services of UIFP; and the “C” group, that UIFP avoid having business with unless with some special agreement. The relationship is not built on contract, but rather on mutual trust. Producers are free to leave if they think that they can get a better opportunity somewhere else. The form of the relationships changed from treating all producers in the same way into individual alliances where, for example, producers benefit in higher price if they produce quality products something that was unthinkable before 1993⁴⁶.

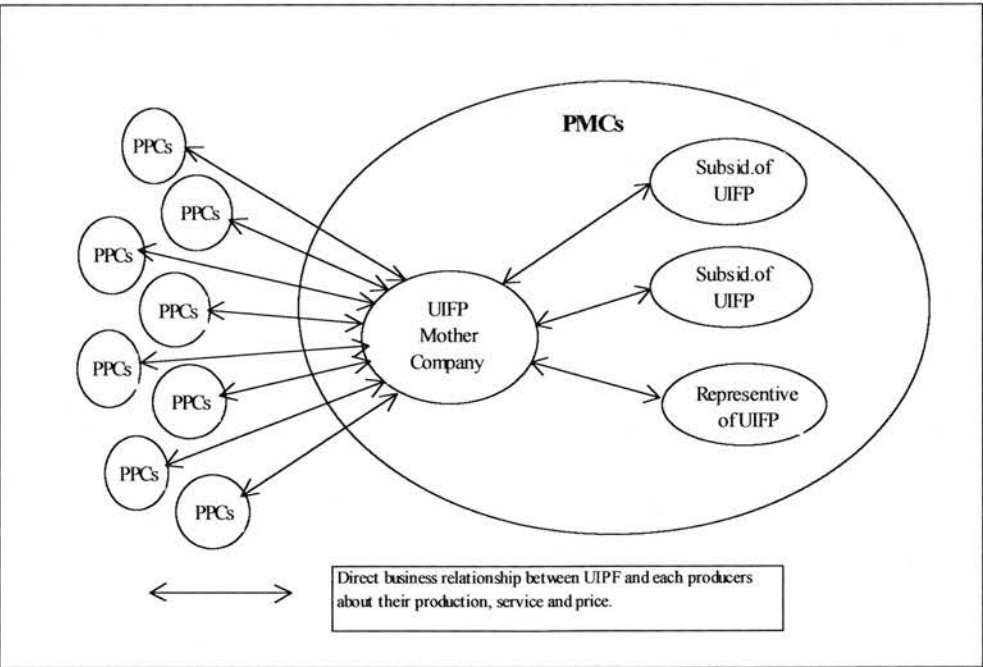


Figure VI.2 Form of UIFP relationship with producers from 1993 – 1999

⁴⁵ Interview with manager of UIFP, I-25.

⁴⁶ Based on interview with manager of UIFP, I-24.

After the change in 1999 the structure of UIFP changed but it had very little effect on the relationship with producers (see figure IV.3). The main effects were on the governance of the network, where the UIFP Mother Company had the role of governing, coordinating and leading the network.

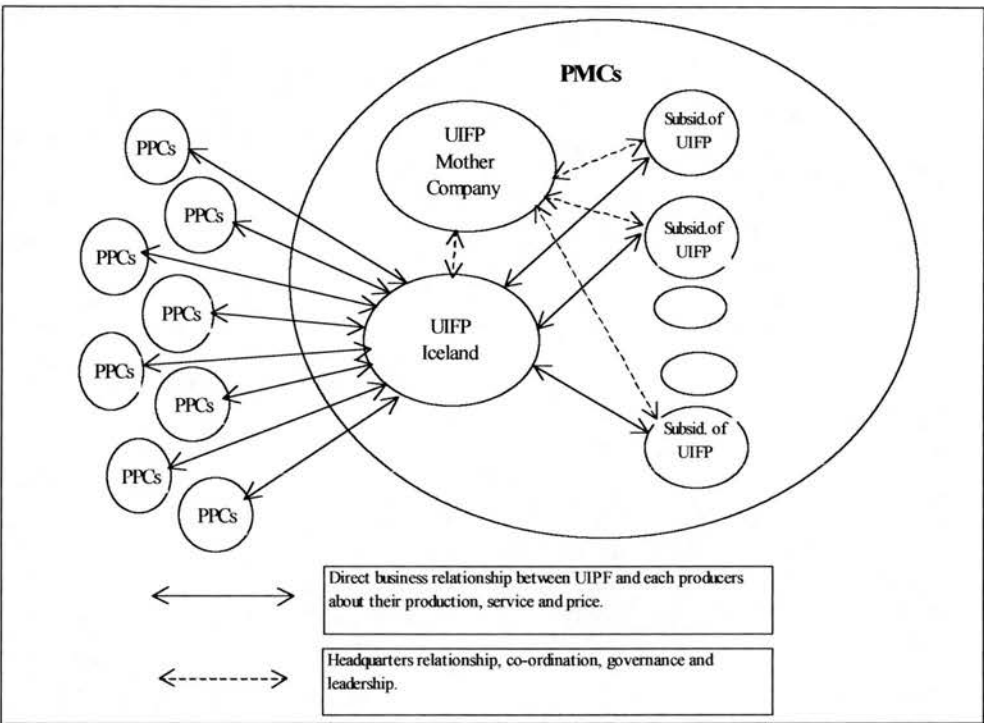


Figure VI.3 UIFP structure 1999-

The first response by interlocutors when they were asked about the nature of the relationship between UIFP and producers after the ownership changes was that it was a clear suppliers/buyer’s relationship⁴⁷. As the interviews went on however it was clear that the relationship included much more than a traditional supplier’s/buyer’s relationship. This is especially true for “A” producers where UIFP provided them with information and service that “B” producers for example, does not get. In addition to this UIFP are committed to buy all the fish from “A” producers at market price, and in the same way “A” producers are committed to sell all their salted fish to UIFP. Hence, these commitments on both sides indicate that the relationship is much more based on alliance than just supplier’s/buyer’s relationships. For other producers such as “B” producers the relationship is much more clearly on a supplier’s/buyer’s basis. It is clear from the interviews with managers and employees of UIFP that they look at the “A” producers as *their* producers

⁴⁷ Based on interviews with managers of UIFP and PPCs.

(for example, one manager talked about “*our producers*” where he meant the “A” producers⁴⁸).

Although the relationship can still be counted as a strategic alliance between producers and UIFP, has moved much closer to a supplier’s/buyer’s relationship than the former sales organisation relationship that it was before 1993. An indication of this is the fact that UIFP buys all the products from the producers instead of selling it through commission sales. Another indication is the ownership of UIFP, which is much more diverse now in 1999 than it was when UIFP Ltd. was established. Although producers still have a majority on the board of the company, other investors such as pension funds and private companies that are not producers have become the biggest owners. It is interesting to see how the ownership has developed from 1993 when UIFP was changed into a limited liability company. Producers have lost their majority in UIFP share: of the twenty biggest shareholders only five are producers have, and they hold only 10,87% of the 52,15% share that these twenty shareholders won in total (see table VI.2). In total, producers count for less than 20% of the total shares in UIFP⁴⁹.

Shareholders ownership 01.06.99	
Ownership of 10 biggest shareholder	38,02%
Thereof producers	8,13%
Ownership of 20 biggest shareholder	52,15%
There off producers	10,87%

Table VI.2 Shareholders 01.06.99⁵⁰

It is clear from these figures that producers no longer own a majority share, or even a ruling share, in UIFP. This declining ownership can in many cases be traced to the poor financial status of producers inside UIFP. In addition to that many producers either stopped production or did not see only point in owning share in UIFP where their influence would be very limited.

Another aspect of the nature of the relationship between UIPF and producers is concentration by the producers, where the number is declining and they are getting bigger. This can be seen from figure VI.4 where the

⁴⁸ Interview with manager of UIFP, I-24.

⁴⁹ Information given be manager of UIFP.

⁵⁰ Útboð og Skráningarlýsing SÍF Júlí 1999. UIFP stock bidding rapport July 1999.

development of the number of producers and their percentage of total export of UIFP from Iceland is shown.

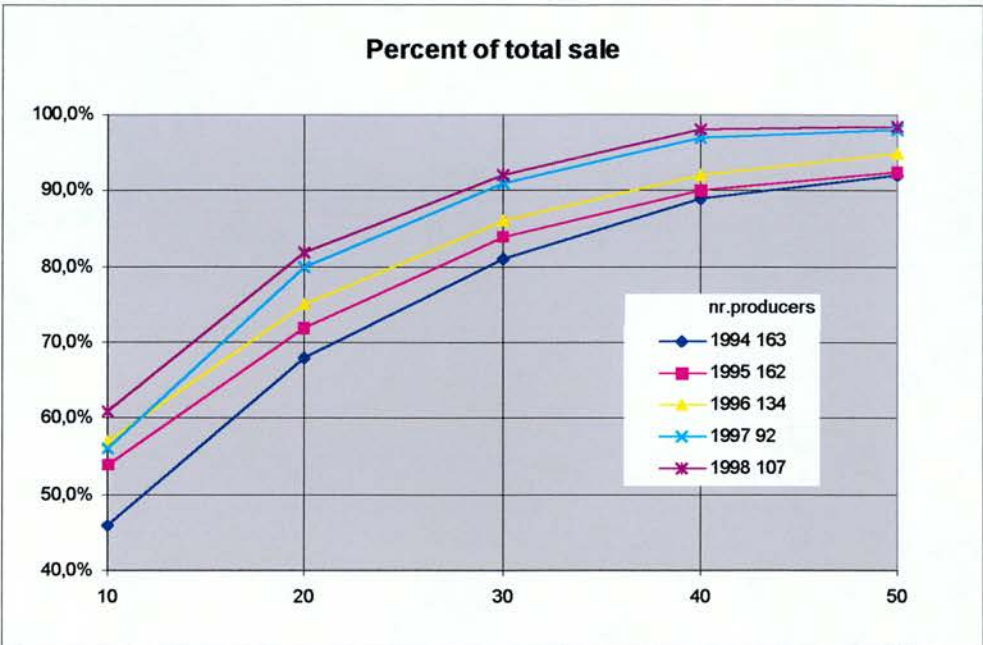


Figure VI.4 Number of producers and percent of total sale UIFP 1194 - 1998⁵¹

From figure VI.4 it can be seen that the share of the 10 biggest companies in the total export of UIFP from Iceland has increased from 1994 when it was around 46 % to around 61% in 1998. Similar can be said of the 20 biggest companies, which in 1998 stood for around 82% of the total export. In 1998 the number of producers associated with the UIFP group was around 107⁵², around 50 of which were “A” group producers⁵³.

The diversification of UIFP into both primary processing and secondary processing abroad and the increased emphasis on other types of products than just salted fish, has also affected the nature of the alliances. It is clear that UIFP is no longer just selling salted products from Iceland but much rather they have created a network of subsidiaries that are involved in “marketing and production of salted and chilled seafood products”⁵⁴. It is therefore a question whether it is not more correct to talk about a UIFP

⁵¹ Information given by manager of UIFP and from stock bidding analyses July 1999.

⁵² In these numbers the smallest producers that use the service of UIFP to grade and pack their product are not counted instead; the packing department of UIFP counted as one producer. Therefore, it is clear that the number of producers in UIFP’s business could be higher although the importance of the biggest would not change much.

⁵³ Based on interviews with managers of UIFP.

⁵⁴ Útboð og Skráningarlysing SÍF júlí 1999. UIFP stock bidding analyses July 1999.

network rather than talking about strategic alliances or joint venture as it was before 1993. Inside this network are then individual strategic alliances between UIFP and producers (at least “A” producers), which then are part of the network. Hence, the nature of the relationship has changed from being strategic alliances between high number of small producers to become much closer to a network with individual strategic alliances between UIFP and producers. Inside this network UIFP can establish strategic alliances with individual producers or others.

In table VI.3, the main factors involved in the network are summarised as they are seen in 1999. The main changes in the last year are the increased emphasis that UIFP has put on primary and secondary processing as well as the integration into distribution of chilled fish products.

		Producers	UIFP	UIFP subsidiaries
Activities	Top level	Managerial, strategy, financial matters	Managerial, strategy, financial matters	Managerial, strategy and connection with UIFP and customers
	Middle level	Day to day activities and information gathering in production, quality and shipment	Selling and connection with customers, subsidiaries and producers	Sale of fish, information collection and connection with UIFP and customers
Resources		Fish stock Knowledge in primary processing and fishing	Brand names Overview over the whole process Marketing information Marketing connection	Brand names Marketing connection Marketing information Secondary processing Primary processing

Table VI.3 Actors, Activities and Resources

The ownership changes and the income of other investors than producers into UIFP have brought the concept of the stakeholder into this network. Although managers of UIFP are not afraid of balancing the different aims of producers and other investors, it is clear that producers are in some cases afraid of too much influence of other stakeholders who could have other interests than those of producers. An example of this is the fact that ten producers formed an occupational organisation (Saltfiskframleiðendur hf.) to buy share in UIFP to react against the influence of outside companies⁵⁵.

⁵⁵ Morgunblaðið 14/06 ‘96.

As previous discussed, the producers have now less than 20% of UIFP shares, so it is clear that they have not succeeded in maintaining their share in UIFP. On the other hand, the majority of producers in the UIFP board indicate that other investors than producers are concerned about keeping some balance and keeping up good relations with producers on more than just a buyer's/supplier's relationship basis.

VI.1.2.1.1 Dependency of actors in the network

Due to the exclusive licence UIFP had on the export of salted fish from Iceland more or less until 1993, producers and UIFP were almost completely dependent on each other. However, this high dependency started to break before 1990 when producers started to sell split partly salted fish mainly to Denmark for further processing. This high dependency affected the relationship in many ways. To UIFP's disadvantage it meant they had duties to serve every producer regardless of their capability to produce salted fish or their strategy. UIFP responded to this by treating producers as a homogeneous group. Many producers felt they were being forced to adapt to UIFP's strategy. Hence, many producers viewed this as enforcement and the relationship missed the necessary flexibility to meet their own aims and strategy⁵⁶. On the other hand these duties put great demands on UIFP and managers often spent lots of their time in making compromises between the different aims of producers⁵⁷.

Around 1992 the Foreign Ministry started to give limited licences for export, breaking this dependency for producers. At the same time UIFP bought a secondary processing plant in France making its operation not completely dependent on Icelandic fish. After 1993 the dependency decreased again by the abolition of the exclusive licence, making producers free to sell their product wherever they wanted. Due to the diversification of UIFP, mainly after 1994, into primary processing, secondary processing and distribution, UIFP has become less and less dependent on the Icelandic producers. In the same way, by the increased number of companies that are selling salted fish and the fact that they are not bound with UIFP, the

⁵⁶ Built on interview with present and former managers of PPCs.

⁵⁷ Interview with former manager of UIFP, I-32.

producers are free and have the option of selling through other companies. Along with this, the traditional markets are in a good condition so there is no problem in selling salted fish today (1999). In difficult marketing conditions however, it is uncertain whether this dependency for producers can increase depending on the abilities of the other marketing companies to sell the products while UIFP are committed to buy all products from group “A” producers. On the other hand producers can become dependent on UIFP services as one manager of UIFP stated.

“Some producers are becoming dependent on our service. Producers in many cases have not the space to stock products and have built up their production in that way that they need to get rid of its productions every week and get it paid. For these producers it could be difficult to change to the old system where they needed to stock their products them selves and capitalise the stocking.”⁵⁸

In a similar way, one employee of a production company selling through UIFP claimed:

“Some producers are become dependent on the financial assistance of UIFP. Where UIFP are starting to finance their fish buy or quota it is difficult for them to leave UIFP and in many cases UIFP has kept them a live by their assistance and service.”⁵⁹

In this way, the dependency between actors in the network depends on the service and financial status of the producers.

From the history it seems that the dependency has been equal for both UIPF and producers. It is clear, however, that it did not matter for UIFP whether one producer did or did not want to sell through them before 1993. Meanwhile producers had no other option if they wanted to produce salted fish but to sell through UIFP. Hence, producers were more dependent on UIFP than UIFP was dependent on them. UIFP subsidiaries, such those in Norway and Canada, are not in any way dependent on producers; it is rather the secondary processing plants in France and the marketing subsidiaries as in Spain that are dependent on Icelandic fish producers. UIFP claims that they are still dependent on the Icelandic fish due to its better quality and

⁵⁸ Interview with manager of UIFP, I 25.

⁵⁹ Interview with employee of PPCs, I-27.

higher selling price than fish from their subsidiaries in Norway and Canada⁶⁰. In 1998 UIFP had over 51% share of the value of the total export of salted fish from Iceland⁶¹. The diversification of UIFP from 1994 was meant to spread the risk in the operation of UIFP by not having to depend on Icelandic producers. Gunnar Örn Kristjánsson, CEO of UIFP claimed in an interview to Viðskiptablaðið (The Business paper) that there was an unacceptable risk during the time when UIFP had to depend solely on Icelandic producers⁶².

VI.1.2.1.2 Conflict of interest and value creation in the network

The vertical integration of UIFP raises the question of whether it could, or has develop(ed) conflicts with the producers in Iceland. First comes the question of the vertical integration of UIFP into foreign producer? This could cause interest conflicts with Icelandic producers who may interpret such integration as UIFP exporting the knowledge and reputation of Icelandic salted fish into countries that have been in hard competition with the Icelandic production. Hence, the buyers that appreciate the quality of the Icelandic fish are not bound to buy just from Icelandic producers but also Norwegian or Canadian. A manager of UIFP claimed this was not the case, but rather what he stated:

*“The fish from our diversification abroad have not the same quality and the Icelandic fish that have special status. In our system it is the cream that floats on the top but there is much more in the cup but the cream on the top and there is difference between markets and different customers some can buy expensive Icelandic fish while others buy cheaper products. By this we are serving different segments on the markets.”*⁶³

This indicates changes in the driving force in the network. Before 1990 the network was completely production driven, where the main aim was to sell producers products. After 1990 this started to change and the UIFP's own value creation starts to be more the driving force for changes. It is though not until after 1993 that this becomes obvious, and after the diversification

⁶⁰ Útboðs og skráningarlýsing SÍF júlí 1999. UIFP stock bidding analyses July 1999.

⁶¹ Útboðs og skráningarlýsing SÍF júlí 1999. UIFP stock bidding analyses July 1999.

⁶² Viðskiptablaðið 27 January – 2 February 1999, interview with Gunnar Örn Kristjánsson CEO of UIFP.

⁶³ Interview with manager of UIFP, I-24.

of UIFP that it becomes explicit, that the main driving force for changes is value creation inside UIFP.

The vertical integration of UIFP into primary processing introduces the danger that UIFP, unconsciously or consciously, puts more emphasis on selling fish from companies that they have ownership in rather than selling products from other companies. A manager of UIFP claimed that there was a conflict of interest when they did not buy all their fish.

“When we both bought and sold products in commission sale there came up conflicts concerning the stocking time. Many producers claimed we put more emphasis on selling our products than theirs. Now we buy all our products and are committed to take all products from our “A” producers so this is no problem today.”⁶⁴

According to producers they do not see this as a problem now. This can in many cases be traced to the marketing condition, that is, there is rather a lack of supply of salted fish, making it no problem to sell the products⁶⁵.

A similar question concerns interest conflicts in the operation of the secondary processing plant and how producers interpret that. The question is, for example, whether the plant will, or have, delay(ed) development of secondary processing in the processing companies in Iceland. From the producers' point of view it can be argued that UIFP put much more emphasis on getting raw material for this production rather than supporting further production in Iceland that could then even be in competition with its own products. In most cases the salt fish products from Iceland are homogenous, and furthermore many production companies are rather primitive. Hence, demands for further processing or value creation is not very high. This makes the conflict between UIFP and producers about value creation not as obvious as for example in the IFPC network; as one manager of production companies said when he was asked about the value creation in UIFP:

“The value creation in UIFP is mainly in the form of that if their operation is efficient they can pay higher price than before. It is clear that the

⁶⁴ Interview with manager of UIFP, I-25.

⁶⁵ Based on interviews with managers of PPCs.

emphasis on the value creation in UIFP network is in their own companies and producers are suppliers for them”⁶⁶

Due to the nature of UIFP and the emphasis on value creation inside their own secondary processing plants, this comment of the producers is in many ways right. In the same way, because UIFP buys all the products for further sale, they are not encouraging producers to produce special products that demand direct connection between producers and customers. In many ways the development of production inside UIFP has been in the other direction than by for example IFPC, as one production manager stated:

“UIFP is always stimulating producers to hand in their products less and less processed. Week old salted fish has not been processed fully and not taken on the colour and texture that it will take after two to three week. Therefore UIFP is taken more and more of the value creation in this process. For many companies this is very good but others want rather to increase their value creation instead of decreasing it.”⁶⁷

In a similar way, a manager of PPC, that has been experiencing in further processing, claimed:

“We tried to sell our products through UIFP and they showed us great interest but our need seemed never be able to go through their system. It is difficult to say what causes this but UIFP emphasis on their own value creation can affect this as well as they buy all their products so this would maybe not fit to their strategy. There is nothing wrong with this strategy of UIFP but it does not harmony with our strategy of increasing the value of our products.”⁶⁸

This change in value creation and the value chain is good for many companies and fulfils their aims towards the production. It is clear though that the emphasis is now on the value creation of UIFP, which in many ways is very well understandable in the light of the demands on UIFP, that is, to make profit and return it to the owners.

This leads to another conflict that interlocutors state is a conflict between shareholders and producers, or as one manager of a production company claimed.

⁶⁶ Interview with manager of PPC, I-19.

⁶⁷ Interview with manager of PPC, I-28.

⁶⁸ Interview with manager of PPC, I-28.

*"I can not see how the demands on UIFP to return as high profit as possible to return to its owner that are no longer producers and the aims of producers can fit together."*⁶⁹

These conflicts between shareholders and producers could be defined as shareholders/stakeholders conflicts and are well known. It is clear from interviews with general managers of UIFP, both present and former, that they were not afraid that although ownership of UIFP would move to groups unrelated to the fish industry, UIFP would still be able to serve its purpose and offer the producers the best price and service. Hence, without offering producers the best price and service UIFP would not be able to make profit to return to the shareholders⁷⁰. The managers seem unanimous that the interests of the two groups of producers and owners are parallel and that it is possible to serve both at the same time. For many producers, especially those who were used to the old days of SIF when profit was returned at the end of the year, this is difficult to admit. Managers of UIFP point out on the other hand that cost awareness has increased after the ownership changes where UIFP returns the correct price immediately, not the end of the year when all the cost has been withdrawn. By this they have cut down the cost of selling the fish and can pay a higher percent of the actual price that they get for their products on the markets. Or as one manager of UIFP stated:

*"For many 'old' UIFP producers this is difficult to adjust to but this is a simple calculation to show them that they are benefiting from this but they missed the time when they had operated their company on the temporarily price and when the payback came in the beginning of the next year they felt that they got bonus."*⁷¹

It is clear from the interviews with both producers and UIFP managers that the interest conflicts are not affecting the relationship today. It is however clear that there are underlying conflicts that could come up to the surface in worse marketing conditions or if more producers moved go into further processing that demands a close connection to the customers which the UIFP system does not offer.

⁶⁹ Interview with manager of PPC, I-28.

⁷⁰ Morgunblaðið 26/11 '93 interview with Magnús Gunnarsson CEO of UIFP 1985 – 1993; and Morgunblaðið 21/05 '95 interview with Gunnar Örn Kristjánsson CEO of UIFP from 1994.

VI.1.2.2 Role of the central firm in the alliance

UIFP has in many ways had a strange position in the Icelandic fish industry. This is due to the exclusive licence of UIFP, which meant that all the different blocks inside the fish industry, such as IFPC, IS and salt fish producers, all met in UIFP⁷². UIFP was therefore not only a central firm in its own network but also central firm in interest matters concerning the general competitiveness of fish processing. Hence it is claimed here that UIFP had two main roles that is, the role inside the network against producers, its subsidiaries and representatives and then the outside role as an interest group for fish producers. This role of acting as an interest group was finally abolished in 1993 except for a moral role, according to one UIFP manager:

“Our voice outside for producers is more a moral one now rather than we are acting as a interest group for them as we did in the past.”⁷³

The interesting part of UIFP role is the internal role both against the producers and the markets. Before the ownership changes, the exclusive licences and the duties associated with them circumscribed the role of UIFP during that time. This can be seen from what the former CEO of UIFP claimed.

“When we had the highest number of producers around 1986-87 we had around 400 producers inside UIFP. Due to the duties that is to serve every producer despite what they produced a lot of our time went into visiting producers to reconcile their different view.”⁷⁴

Due to this, much of the effort of managers of UIFP went into coordinating activities and the different aims of producers. As an example of that one interlocutor that worked inside UIFP around 1990 claimed it was not easy to convince the producers of buying Nord Mure, the secondary processing plant in France⁷⁵.

⁷¹ Interview with manager of UIFP, I-25

⁷² Interview with former CEO of UIFP, I-32.

⁷³ Interview with manager of UIFP, I-24.

⁷⁴ Interview with former CEO of UIFP, I-32.

⁷⁵ Interview with former employee of UIFP, I-32.

Selling of the products has always been coordinated inside UIFP. The UIFP took care of all the communication with the representatives and later subsidiaries on the markets, and also sold products direct to customers. After the diversification of UFIP and establishment of marketing subsidiaries, the UIFP in Hafnafjörður still has a role in selling products. This is, for example, to Spain to producers that see UIFP subsidiaries in direct competition there. Also, all selling to Portugal is done from Hafnafjörður⁷⁶. Due to that the interface between producers and UIPF is all through the marketing division of UIFP, and later UIFP Iceland. The role of the marketing division of UIFP was to take care of both buying products from producers as well as selling them on to the markets. After the changes in 1999, UIFP Iceland took over the role of the old UIFP as the connection to producers and the marketing operation. This role of UIFP Iceland includes reporting information from markets to producers. This is done through the channel of the central firm and in a way cuts out all connection between the producers and the markets. This simplifies the connection between the producers and UIPF and it was interesting that interlocutors were not concerned about that, as can be seen from this quotation in an interview with one manager of PPCs:

“We concentrate on fishing and processing but the sale is in the hand of a company that has good overview over complicated marketing activities.”⁷⁷

There the manager is referring to UIFP. It is however clear that producers have the need to follow the marketing situations so they can base their production decisions on the development in the markets. This information is distributed from the central firm in the form of newsletters, personal contacts and the service people from UIFP that travel between producers (mainly “A” group producers).

Before 1993 UIFP was the marketing division of producers in that sense that they sold their products more or less all in commission sale. Due to the exclusive licence nothing was done on the markets without UIFP doing it. This put pressure on UIFP to be the leading firm in the network as they had

⁷⁶ Interview with manager of UIFP, I-24.

⁷⁷ Saltarinn 3. tbl., 5. árg., 1998. Interview with Pétur Pálsson manager in Vísir hf.

the connection with the markets and exclusive licences to sell there. On the other hand UIFP was dependent on producers for products and on all major investment or strategically changes. Thus the role of UIFP before 1993 was to “serve producers” needs, making the network product driven much rather than marketing driven. UIFP has definitely been leading the network in many matters. This is visible in all kinds of quality matters concerning production, and in interest matters. In the same way the governance role of UIFP in the network before 1993 is obvious and can be seen from the importance of co-ordinating activities in the network. Hence the main role until 1993 was to serve producers and govern the network.

The ownership changes on UIFP and the abolishment of the exclusive licence changed also the role of UIFP as the central firm in the network. After these changes UIFP was on the free market and producers were no longer forced to sell through UIFP. This has made it clear both to UIFP and producers that there is free competition on the markets, as Gunnar Örn Kristjánsson CEO of UIFP claimed.

“UIFP operates now under the law of the markets. We are in full competition with other exporters about producers’ products and we have to be competitive in that competition. Our future is based on that producers find motivation to be in our business. The producer chooses the exporter that returns best service and best return. This is vice versa UIFP can if that is the case refuse to take producers in our business.”⁷⁸

After 1994 UIFP stopped taking on products in commission sale and started to buy all their products for further sale or production. Gunnar Örn Kristjánsson claimed in an interview with Viðskiptablaðið (Business paper) that:

“Commission sale can not work if we are operating company on the free stock market. Investors’ demands return on the capital that is bound in the company. It is very difficult to return when companies are almost only operating on commission bases. If company is going to be operating on commission bases I find it more appropriate to operate the company as a sale organisation in Co-operative bases in ownership of producers and not to have them on the free stock market.”⁷⁹

⁷⁸ Saltarinn 2. tbl., 2. árg., 1995. Interview with Gunnar Örn Kristjánsson CEO of UIFP.

⁷⁹ Viðskiptablaðið 27 January – 2 February 1999, interview with Gunnar Örn Kristjánsson CEO of UIFP.

According to the UIFP CEO the ownership changes have demanded that the company can no longer operate on commission bases or act as a marketing division of producers. Hence, the role of UIFP has changed. It is no longer there to serve producers but to be competing with other marketing companies for their business. According to the CEO of UIFP, they do this by offering producers competitive price and good service⁸⁰. Still UIFP as the central firm had the role to take care of all the relationships with producers in the day-to-day activities, and to co-ordinate the activities between the markets and producers in sales matters. The main change is that UIFP gets new demands of profit, which they respond to by increasing their own value creation and by diversification where they use their formal knowledge of markets. Hence, the central firm has increasingly the role of strategically leading the diversification of their constellation. For producers this means that they still have more or less to adjust to UIFP's strategy rather than UIFP compromising between their different strategies. The same can be said about the governing role of UIFP: that is, its emphasis is more on the internal in the constellation instead of the external against its producers. The changes of the relationship with producers have simplified the role of UIFP against the producers. Now it is more about being competitive instead of having duties to serve all and be responsible for governing, leading and coordinating all activities that were connected to the marketing operation.

The separation of UIFP operation in Iceland into the UIFP Mother Company (MC) and UIFP Iceland clarified better the different role of UIFP. After the changes, the governance of the networks and strategy leadership moved to UIFPC MC. UIFP MC has no core activities on their shoulders; much rather it acts as a traditional headquarters with the responsibility of co-ordinating activities and strategy of the UIFP subsidiaries. Included in this are matters as co-ordinate accounting, information systems and computer systems⁸¹. Then UIFP Iceland is responsible for the operation in Iceland, with the main emphasis being on the relationship with producers that is, to

⁸⁰ Viðskiptablaðið 27 January – 2 February 1999, interview with Gunnar Örn Kristjánsson CEO of UIFP.

⁸¹ Based on interviews with managers of UIFP.

coordinate the day-to-day activities concerning the buying and selling of the products as well as the service.

VI.1.2.3 Governance of the network

The governance of the UIFP network has changed in harmony with the changes to the network in 1993 to 1994. After the changes in 1994 the governance of the relationships with producers has moved closer to a supplier's/buyer's relationship than before that time. It is, however, though very interesting how UIFP has tried to maintain social connection with its producers.

VI.1.2.3.1 Mechanism

The governance before the ownership changes was based around UIFP, which took care of all the marketing activities. In the same way, it was UIFP's responsibility to coordinate all activities that were included in the marketing operation. Hence, the mechanism during this time was based on centralisation by UIFP. In coherence with this centralisation, direct connection between producers and the markets was not practised. In many ways this is understandable due to the often high number of producers and the little quantity they produced. This centralisation has caused clear separation of activities in the value chain. Producers are not meant to have direct connection to the markets, as an employee of PPCs claimed:

*"I once tried to contact a sales man of UIFP that I knew to get information from the markets. I just got the same response as I got from UIFP in Hafnafjörður. It is clear that they were not allowed to give more information."*⁸²

Due to the centralisation and high number of producers the mechanism seems to have worked fairly well. There were little evidence of producers avoiding the centralisation and interference of the central firm, and, according to managers inside UIFP, this centralisation has remained over the operation time of the union and they have not noticed any need from producers to operate differently⁸³. After UIFP started to buy the products

⁸² Interview with employee of PPC, I-27.

⁸³ Interview with managers of UIFP, I-24 and I-25.

this has not been a relevant question, but producers still want to follow what is happening on the markets. A manager inside UIFP claimed, though, that they watched out for changes and developments in the relationship with producers:

“With more concentration by producers where they are becoming bigger their needs and aims can change. This can cause that they want increasingly to be more involved in the marketing activities and to be connected to customers with further processing in mind similar what has been happening in the frozen fish. If this will be then we will have to face it and adjust our system to that but this is not happening today.”⁸⁴

The mechanism of UIFP does not offer many other options for producers than to be a supplier that is; UIFP buys the products from producers for further sale. Despite this separation, UIFP tries to inform “A” producers about the marketing conditions and changes on the markets.

This clear separation of activities can be claimed to be economical for the network as a whole due to its simplification of the relationship and coordination of activities, which both bring down the cost of selling in the network. On the other hand, this opens up the possibility of a lack of understanding of the needs and expectations of actors in the network. One former manager of a production company took an interesting example of what can happen in this case. This producer was producing stockfish, which UIFP was also selling.

“In Iceland we have always graded the skinned fish as the lowest quality and therefore got the lowest price for it. When we were travelling in Italy visiting customers we meet an Icelandic salesman selling fish from Norway our main competitor there. This Icelander informed us that the Norwegians graded the skinned fish in special group and sold it to Northern Italy for top price. The company that this Icelander worked for used the same representative as we did. This representative never returned this to us or at least our sale organisation never told us about it. Later we found out that the customers in North Italy bought the lowest quality from Iceland and it was as a lottery to see how much of skinned fish they got. The next year we graded the skinned fish specially which returned us around 3% higher price for the whole production that spring”⁸⁵.

⁸⁴ Interview with manager of UIFP, I-24.

⁸⁵ Interview with former manager of PPC, I-12.

Although this example is not taken from UIFP, they used the same grading system and did not change it until after this. This is a good example of how a distancing of the relationship between production and marketing can create barriers against learning and value creation, which both emerge from good understanding of each other's needs and expectations.

One interesting aspect of the governance mechanism is the board of the subsidiaries. Producers are in the majority of the board of UIFP MC that then nominates the boards of subsidiaries. Hence, in 1999, producers are in the majority in the boards of subsidiaries. The CEO of UIFP is the chairman of foreign subsidiaries, and the general manager of UIFP Iceland is the chairman of the board of the subsidiaries in Iceland. According to a manager of UIFP, this is done to maintain good relationships with producers⁸⁶. In this way, UIFP has the option of building up the trust of the producers in the operation of UIFP abroad. Coordination of the operation of the subsidiaries is gained by the fact the CEO of UIFP MC and General Manager of UIFP Iceland are the chairman of the boards as well as other members of the UIFP board are in majority of the boards of subsidiaries. Theoretically this introduces the possibility that UIFP MC can lack formal authority over its subsidiaries. This is unlikely however, due to the fact that members of the UIFP MC board are usually in the majority on the board of its subsidiaries. It is, in a way, strange that the boards of the subsidiaries are not executive boards of managers of UIFP MC and managers of each subsidiary. This indicates the tendency of UIFP to maintain good connections with producers and to involve them in the governance of UIFP even though UIFP is not acting as their sale organisation any longer.

Although the mechanism of governing the UIFP network is built around the central firm and centralisation personal, social contacts are an important part of the mechanism⁸⁷. Before the ownership changes managers of UIFP claimed that a lot of their time went into making compromises between the different views of producers, and a lot of their time went into visiting producers as well as personal contacts. After the ownership changes UIFP

⁸⁶ Interview with manager in UIFP, I-24.

⁸⁷ Interview with former manager of UIFP, I-32.

has maintained the personal contacts and social connection. This can be seen from the previously described domination of producers on the board of UIFP and its subsidiaries, as well as the gathering for producers after annual meetings, trips for producers and marketing meetings for producers. In addition, UIFP does not have contracts with producers but the relationship is based on trust and the will to be in each other's businesses. Despite all this, it is clear that one of the main characteristics of the governance mechanism of UIFP and the interaction between producers and UIFP is an inflexibility to meet the different needs of producers.

VI.1.2.3.2 Power

Formal authority was for a long time in the hands of producers. Until the ownership changes, producers had the formal authority in the network and producers dominated the board of UIFP. Equality between members, together with the high number of members, made it difficult for a small group of members to gain a dominant position. Through the centralisation of activities and information from the markets it is unquestionable that UIFP gained much informal power or authority in the process. This was primarily authority over the day-to-day activities of sales. As an example of how some producers viewed this authority, the following quotation is taken from an interview with a manager of a production company that sold through UIFP:

*"Inside UIFP I felt like I was enchained. It was either to lay down and give up or rise up and try to break the concatenations away."*⁸⁸

According to this producer and others it is clear that if producers had to follow the UIFP sale strategy they did not have any other options. This also reflects the lack of flexibility that has characterised the interface between UIFP and producers. On the other hand former manager of UIFP pointed out that, due to the separation of activities, producers often placed unrealistic demands on UIFP, which were almost impossible to follow⁸⁹. Producers had the formal authority due to the ownership that is, UIFP was their sale organisation. During that time producers had to agree on all major

⁸⁸ Frjáls Verslun interview with Sæunn Axels.

investment, limiting the independence of UIFP and its authority to overtake the governance and dominate the network. Hence the formal authority was in the hand of producers but the informal authority was in the hands of UIFP.

After the ownership changes, the situation has altered such that owners other than producers have gained a majority share in UIFP. Hence, shareholders have gained the formal authority of UIFP, which they have then assigned to their representatives on the board (that still are, in the majority, producers). The individual producers have no longer formal authority to stop investment, and all equality has been abolished. UIFP itself has also gained much more authority in the process, both in its business with producers as well as in fulfilling its own strategy. It is clear that UIFP has used this increased authority to change its operation in accordance with the new demands on its operation from shareholders, but this has been to return profit on its operation.

VI.1.2.3.3 Strategy

Before the ownership changes in UIFP it is in many ways difficult to point out a strategic leader in the network. From 1957 producers started to have much more impact on the strategy, which held until 1990. From that time the strategy of UIFP started to change rapidly and move more towards the interest of the owners and the independent interest of UIFP as an individual company. The strategy from 1993 seems to be focused on the interests of shareholders, and producers are best served by UIFP having more independence and playing a bigger role in the international business of salt fish instead of isolating itself with Icelandic producers. In that way UIFP could use its knowledge, connections and its competitive strength to sell fish from other nations, and in return bring that back in the form of profits that could be returned to shareholders and thus benefit other producers through higher prices and better service. Hence, it is clear from the ownership changes in 1993 that the strategy of UIFP has changed and the emphasis has moved, from just bringing the producers the highest price, to making profit that can be returned to shareholders.

⁸⁹ Interview with former manager of UIFP, I-32.

Before the ownership changes, UIFP was a rather conservative organisation. This is in accordance with the products that it has been selling, which are traditional foods in most of the markets countries. It is also in accordance with the nature of the organisation, that is, to be a sale organisation for producers, built on equality, where it is difficult for one or a few companies to become strategic leaders. The strategy of UIFP for most of its time was to serve members and sell their products. UIFP had however also led certain changes in quality as well as in R&D. It is claimed, though, that UIFP lacked strategic leadership during most of its operation time where the main strategy is to serve its members and sell their products. An example of this can be seen from the following quotation:

*"It is difficult to say why UIFP did not build up stronger position on the markets when they had the exclusive licences to sell on the markets. It seems that they were too occupied to sell products rather than built on strong position on the markets."*⁹⁰

It was not until 1990, when UIFP bought Nord Mure in France, that it could be said that UIFP started to lead real changes in the network. This changed after the ownership change when UIFP started to take on clear leadership in its diversification of the network's operation. It has to be considered, though, that UIFP lost around half of their export from Iceland to other competitors. This of course led them to look elsewhere for increased business, or as a manager of UIFP stated:

*"Now we export around 50% of the total value of salted fish products from Iceland. We are not looking for some certain percent of the total export rather we are looking for good producers and return on our operation. We have no intention to build up some Empire and some dominance approach to producers. Some producers are such that we do not want to have them in our business and fighting for higher percent would be much too expensive."*⁹¹

The period 1993 - 1998 is characterised by a transformation of the company, from a "sales organisation" for Icelandic producers to an "international marketing and production company in chilled fish production"⁹². It is

⁹⁰ Interview with manager inside UIFP, I-24.

⁹¹ Interview with manager inside UIFP, I-24.

⁹² Taken from UIFP strategy on www.sif.is.

interesting to observe how the strategy of UIFP is always changing more and more into marketing and production of chilled fish products. Salted fish is of course a chilled product, but it seems to be clear from documentation from UIFP that the emphasis is always moving from mentioning salted fish products to chilled product. Hence, this opens opportunities for UIFP's operation to become much more diverse than it is now and indicates strategic changes, where the emphasis will be on all sorts of chilled products instead of salted fish.

It is difficult to judge the impact that strategy has had on the governance of the network. Before the ownership changes the strategy of UIFP was to be a service unit, not to lead the network in strategic ways. After the ownership change the strategy becomes clearer as well as the relationship with producers. The strategy is to buy all products, which makes the governance much simpler than before, but the governance of UIFP has opened up to allow the possibility of meeting different strategies of producers.

VI.1.2.3.4 Social maturity and trust

One of the most interesting parts of the governance of the UIFP network is that although the relationship has moved more into business-to-business relationship, UIFP has put great emphasis on the supportive and social aspect of the relationship. As an example of this, a manager inside UIFP pointed out that after the ownership change the new general manager planned to abolish the tradition of inviting producers to a big gathering after the annual meeting in 1994. Members of the board could persuade him to change his mind and hold the party⁹³. In the same way, UIPF invited producers to France when they reopened their secondary processing there. This manager inside UIFP claims it is just part of building up a good relationship with their suppliers. It is also clear that many of the producers are, and have been, very loyal to UIFP and claim that they are "*UIFP men*". Hence, there are many social links/ties, both between producers inside UIFP, and between UIFP and producers. UIFP has increasingly used this, and, as a manager of UIFP claimed, this will even be increased in the future by the change of UIFP MC and UIFP Iceland.

VI.1.3 Conclusion

Until 1993, the UIFP network operated as a formal joint venture that was enforced on the participants through the monopoly that UIFP had on the export of salted fish products from Iceland. The development after that has been in the direction of informal alliances between UIFP and each producer. This development into informal alliances that are not based on contracts, but rather on trust and personal relationships between actors, is in accordance with, and supports, what has been pointed out in the literature about strategic alliances and network where the tendency is to have much more informal relationship instead of strict contracts⁹⁴. After the ownership changes, UIFP tried to establish contracts with producers but soon gave up due to the complexity and difficulties in maintaining them. This supports Grandori, where she claims that the establishment of formal contracts is too expensive and complicated⁹⁵.

Abolishing the monopoly that UIFP had on the export of salted fish products in 1993 brought new factors into the network. First of all it brought competition into the network. Until then, competition was almost unknown. According to most of the interlocutors inside UIFP, they put much emphasis on competition and on the fact that they are now operating in a free market. According to the analysis of the relationship that UIFP has with its producers, it is clear that UIFP is operating strategic alliances with its “A” producers, and is a free market with “B” and “C” suppliers. This supports the use of the two dimensional scale put forward by Ouchi, where the relationship UIFP has with its producers is on the marketing side of the scale the “A” producers in the strategic network on a Win-Win strategy: and the “B” producers on the Classic Market, where the relationship is based on ad hoc relationships⁹⁶. Before the ownership changes, UIFP was operating much more in the clan section on Ouchi’s scale, where the relationship is built on hierarchy methods but the strategy was a win-win strategy for all

⁹³ Interview with manager of UIFP, I-24.

⁹⁴ See for example Devanna, A. A. & Thichy, N.; Grandori, A.; Lorange, P & Roos, J.; Killing, P. J.

⁹⁵ Grandori, A.

⁹⁶ Jarillo, C. J.

participants. Hence UIFP now is operating in a free market both in its export and in buying products, but it is obvious that with their key suppliers (the “A” suppliers) they build their relationship on cooperation or strategic alliances. This conclusion supports Axelsson when he claims that the environment should not be viewed as totally faceless and completely competitive: rather, it should be viewed as a mixture of cooperative and competitive environment⁹⁷. It is clear from interviews with managers of UIFP and producers that they recognise this although, in public, they put most of the emphasis on competing in a completely competitive environment.

It is clear that the competition has brought around changes in a rather conservative or even stagnated network, as UIFP was before the ownership change. Now actors can evaluate their options with other methods of selling and have the option of leaving the network, which was unknown before 1993. The other factor that the ownership changes brought into the network was stakeholders in the form of shareholders who were not producers. This caused concern to many producers that this would change the operation of UIFP in such a way that it would not benefit them any more. Conflict between these two types of stakeholders, that is shareholders and producers, have not been very visible, but clearly UIFP has sharpened up its strategy and aims (that is, to return profit for its shareholders). In favourable marketing conditions for UIFP, as they have been, this is not a problem, but in a more difficult situation there is the danger that the short term view of shareholders will not be parallel with producers’ aims.

An interesting part of the diversification of UIFP is its strategy to take care of almost all of its sea transportation by buying the cargo ship that had previously taken care of its transports. In this matter UIFP seems to be moving in an opposite direction to many of today’s companies, which is to concentrate on the core business and let other companies take care of peripheral businesses⁹⁸. By this UIFP controls the main transportation of its

⁹⁷ Axelsson, B.

⁹⁸ See for example Hamel, G. & Prahalad, C. K., 1994.

products that, as claimed, can make them more efficient and economical⁹⁹. This also indicates the strategy of UIFP to control as much of the value creation and cost in their network as possible. This started to change in 1990 when UIFP bought the secondary processing plant in France then starting to add value by secondary processing to the products, which they had previously just sold. After 1994, when UIFP started to buy all the products itself and increase its diversification into primary processing and secondary processing, the focus moved completely to their own value creation. Hence, the strategy of UIFP has changed in the way they control their own supply chain where they are involved in almost all the steps of the chain. In a way this contrasts with the trend in the supply chain management where the emphasis has been on building competitive supply chains through cooperation as described earlier in chapter IV describing market developments and in chapter V, Literature review¹⁰⁰.

These changes to the UIFP value chain mean that UIFP's competitive stance against producers and other exporters is built on its ability to create value in a more effective way than other competitors and then return higher prices and better service than its competitors. Hence, they create value for the producers through their own constellation. From the producers' point of view this is fine as long as they are not motivated to go into further value creation themselves or to go closer to the consumers in the markets. Then the system for value creation inside UIFP would not be the right channel for those producers.

The governance of the UIFP network has for all its operation time, been based on centralisation. The reason for this can be traced to the homogenous products UIFP was selling and the high number of producers inside the network. Therefore the central firm in the network has played a major role in the process. This role has mainly been to coordinate the activities through the markets and through production. The role of the central firm has also been in leading changes in the network such as

⁹⁹ Saltarinn 1. tbl., 4. árg., 1997. Interview with Jón Rúnar Halldórsson sailing manager

¹⁰⁰ Cook, R.; Fearne, A. & Dedman, S.; Wysocki, F. A.

improving quality, processing methods and packing. Later the role was also to act as a pressure force for producers in interest matters.

The governance mechanism of UIFP before the ownership changes was inflexible and conservative. It can be argued that it needed to be conservative with so high a number of small producers, many of which would have difficulties keeping up with fast changes. This, however, raises the question of why the mechanism and the environment of UIFP had to be so conservative and even stagnated? One explanation of this may be that UIFP had no formal authority over its members except through its monopoly and access to the markets. Despite this it is clear that UIFP built up much more power in the process by controlling resources such as the day-to-day marketing activities. These day-to-day activities included the control over the brand names and the marketing know-how. This supports Pfeffer's conclusion when he claims that power in a network often arises from centralised control or coordination over other participants in the network¹⁰¹. This suggest that the informal power that is gained by this is much more active than the formal power that is based on companies' constitutions and is really only exercised at the annual meetings. This also suggests that there has been a power struggle in the network, where the UIFP, as a central firm, has built up its position in the network through coordination and control to overcome the lack of formal authority. This power struggle and lack of authority, which meant that UIFP had to get producers' approval for all major changes, could have led to stagnation in the network, whereas compromises between the producers would not be a very quick way to respond to changes. This can be interpreted as a lack of clear ownership in the network, where the equality and high number of owners before the ownership change has caused it to lack vision and strategy. After the ownership change the strategy and ownership structure of the network is much clearer than before.

There was very limited indication of existence of an informal governance mechanism that was boycotting the formal centralised mechanism. This can be traced to the homogenous product and the often-small size of producers.

¹⁰¹ Pfeffer, J., 1992.

Producers have showed limited interest in further value creation that demands more direct contacts to the markets and customers there. From the analysis it is clear that, although the formal mechanism is built on centralisation and standardisation, the personal contact and trust are still major factors in the relationship between UIFP and producers. This is especially interesting to see after the ownership changes, when many said that the “old” time of social relationship had been abolished. It is clear that, although the relationship between UIFP and producers is more based on a business-to-business relationship than it was before the ownership changes, UIFP has put greater emphasis on their social relationship with the producers, and that they are “UIFP men”: that is, almost a part of a family. It could be claimed that this is to develop or maintain a good relationship with the suppliers (the producers) and, in accordance with the previously described view of cooperation in the supply chain, to make it more competitive. Hence UIFP is consciously working on building up UIFP culture (that is understanding and trust between the two sectors) in order to improve the relationship. This supports the literature on strategic alliances and networks, where, as Nam¹⁰² and Doz¹⁰³ point out the danger of different national cultures can jeopardise the alliances. In UIFP it is not national culture but differences in the cultures of companies that are operating in the international market and the often-local small companies in Iceland.

The lesson that can be learned from the UIFP case is that, for a network like UFIP, which stretches over many levels in the value chain, it is important that the central firm has the defined role and necessary authority to lead changes in the network environment so it can fulfil the owners’ needs. Otherwise it is likely that this will lead to a power struggle between actors in the network that can cause the network to become stagnated, as in the UIFP case. The history of the UIFP network also suggests that clear ownership of the network is necessary to bring clearer aims and authority into the network.

¹⁰² Nam, H. S.

¹⁰³ Doz, L. Y.

VI.2 Icelandic Freezing Plant Corporation

Sölumiðstöð Hraðfrystihúsanna, the Icelandic Freezing Plant Corporation (abbreviated IFPC), was established in February 1942 after the companies in the freezing industry, that were privately owned, decided to leave the Fiskimálanefnd (the government owned institution) that took care of their sale activities. Behind the establishment of the IFPC were 15 companies, and more joined in the next weeks so the total number was around 22 companies.

VI.2.1 History and development

VI.2.1.1 1942 - 1962 Establishment and Entrepreneurship

The ownership form of IFPC in the beginning was a Co-operative among the producers. This is, in many ways, strange, considering that the producers' companies were all privately owned and that most of them were in limited liability form. A rather strict law from 1934 can explain this to some extent: Fiskimálanefnd was allowed to can grant producers' licences to take care of their sales if they established an organisation that fulfilled certain requirements concerning ownership. Another explanation is the taxation law in Iceland at this time. It was difficult to build up funds inside the companies without having to pay taxes on them. Hence, the producers argued that they had already paid taxes on the turnover of the fish in the processing, and having to pay taxes of their selling would be double payment of taxes. To avoid this, and to fulfil the previously- mentioned legal requirements, the aim of the company was to sell members' products in commission sale and to be a non-profits company in the sense that profits would be paid back to its owners. To bring light on the objective of IFPC it is necessary to look at the first law of the company from 1942, some highlights of which are¹⁰⁴:

- The objects of the company is to sell marine products produced in members' companies, on foreign markets to take care of necessary purchases for the members' companies, to look for new markets and

¹⁰⁴ Hannibalsson, Ó. & Einarsson, H.

to experiment with new products and production methods in the companies.

- Members can only be those who operate freezing plants and they have to obey the law of the organisation and its legal agreements.
- Members have to hand over all their products to the organisation to sell and they are not allowed to sell themselves or have others to sell the product of their freezing plants. Failure to fulfil this requirement can lead to a penalty.
- The organisation is allowed to have control over the production of its members to guarantee the quality of the products.
- To cover the operational costs, the organisation takes 1% of FOB price of sold products from its members. In addition, the organisation is allowed to add a levy on the price of accession that it sells to its members' companies.
- Profits of the organisation will be split between its members in proportion to the percentage of export value of each member's companies.
- Each freezing plant has one vote at meetings of the organisation.

From the first law it is obvious that great emphasis is placed on the equality of members, as indicated by the paragraph that each member had one vote. Other interesting characteristics of IFPC are the Co-operative ownership and the fact that the company is supposed to be a non-profit organisation. This indicates that IFPC was in the beginning just meant to be a commission-based sales organisation for the producers and not be involved in any other operation.

IFPC opened its first sale office abroad in the US in 1945. In 1947, it then changed the form of the sales office into a subsidiary, Coldwater Seafood Corp., that was a US company fully owned by IFPC. In 1954, Coldwater established a secondary processing plant in Maryland US to produce coated fish sticks made from raw material from Iceland. This was the first secondary processing plant owned by IFPC. With the establishment of the subsidiary in the US, IFPC set the strategy that it has followed, in the most part, since. The main aims of this strategy were to get as close to the customers as possible by establishing subsidiaries in local markets, and to use its own brand name to build up customers' loyalties to the brand. It is clear though that changes in the retail sector over the last two decades, with the increased importance of supermarkets and their own brand names has

impacted on this strategy of IFPC. Hence, an increased quantity of IFPC production now goes into supermarket brand names.

Other highlights in the history of IFPC during this period include:

- 1946 Sales office in Amsterdam opened. This was closed in 1949
- 1948 Sales office in Prague opened. This was operated until 1953 when it moved to Hamburg.
- 1953 Sales office opened in Hamburg and closed again in 1956 when the operation moved to Prague until it was closed in 1960.
- 1955 Snax Ross Ltd., a Fish and Chips company in the UK, was bought and started its operation in 1956. In addition, in 1956 IFPC established secondary processing plants in the UK under the name Frozen (Fresh) Fillets Ltd., which started operation in 1958 but was closed down in 1962.

The governance of IFPC until 1962 is more or less in the hands of the board, where the chairman and vice-chairman acted more or less as the chief executive for the company. In addition, the board was involved in operational decisions by normally having meetings at least once a week. In 1954, IFPC operations were split into two sectors: operation of the company in Iceland, and the sale and market sector. Each sector then had a manager who was responsible for its operation and was directly under the board and its chairman.

Around 1960, the freezing industry faced increased operational difficulties at home, and, in addition, payments from the main market in the US were delayed due to the time consuming sales process and increased stocks in the US. In addition to this delay, it became obvious that Coldwater paid 10% less for the products than the main competitor from Iceland, the Co-op Federation. This was due to difficulties in the operation of the secondary processing plant, causing them to pay the producers in Iceland a lower price. Hence, producers were in fact paying for the loss of the secondary processing plant by lower prices¹⁰⁵. All this, together with an increased dissatisfaction with the governance and effectiveness of the operation of IFPC, led to changes in governance and the management team of IFPC around the annual meeting in 1962.

¹⁰⁵ Hannibalsson, Ó. & Einarsson, H.

Operation of IFPC during this period had increased and changed dramatically, and it was clear that IFPC was much more than a commission sale organisation without assets. During this time, IFPC owned warehouses, office buildings, and a secondary processing plant. Hence, it was necessary for IFPC to have an independent financial status separated from its owner, to present to banks and other companies and institutions. As an example of how IFPC operated during this time, IFPC bought Snax Ross Ltd. UK in 1955 and the U.S. subsidiary of IFPC, Coldwater, had to pay the price because IFPC itself did not have any assets or profit¹⁰⁶.

All this created pressure for changes in both the structure and governance of IFPC, as well as in the financial funding of IFPC. The aim of these changes was to increase the decentralisation and flexibility of the organisational structure to ensure the operation was more effective. The main changes were¹⁰⁷:

- The operation was split into three sectors'; each with its own manager; sale and markets, production and a financial sector. The three managers, as well as the chairman and vice chairman of the existing board, formed the executive board of the company that also included the operation of subsidiaries abroad. The chairman of the board worked in IFPC.
- The country (Iceland) was split into seven production areas, each of which had one full member of the board and one alternate member, and the board would meet at least once per month instead of once a week. Each area got one member and then the chairman and vice chairman of the board would be voted separately, so the board would have nine members.
- A special equity fund was established to ensure that IFPC would have a stronger financial status and not be as dependent on its owners as before.

In the history of IFPC it is claimed that, as an organisation, it had probably never been as close to collapse as during the period of 1960 – 1963, and if the changes that were made then had been un-successful the future of IFPC would have been uncertain¹⁰⁸. The changes of IFPC in 1962 were for most

¹⁰⁶ Hannibalsson, Ó. & Einarsson, H.

¹⁰⁷ Hannibalsson, Ó. & Einarsson, H.

¹⁰⁸ Hannibalsson, Ó. & Einarsson, H.

part unchanged until 1985¹⁰⁹, with the exception that the financial manager was made a general manager or chief executive in 1969.

VI.2.1.2 1963 -1982 Growth and expansion

After the changes in 1962, IFPC was granted much more independence from the producers than it had before. This made IFPC much better qualified to cope faster and better with the changes in the business environment and expansion its own. Professional managers were now the ruling actors in managing IFPC instead of the board interfering with daily matters. There were three general managers of IFPC, all working on the same level. In order to bring the board and the managers of IFPC closer, a managers committee was established. Its role was to take care of operations between the board meetings (that were now held around once per month, instead of at least once per week). The managers committee comprised the three managers of IFPC and the chairman and vice chairman of the IFPC board¹¹⁰. It was not until 1969 that one manager was promoted to become president of IFPC instead of three managers. Then Eyjólfur Ísfeld, who had been the financial manager of IFPC, was promoted as president. Other managers held on to their jobs, so the changes only resulted in having one manager or president responsible over the whole operation¹¹¹.

One of the main aims of IFPC during the first part of this period was to build up the infrastructure of the company to cope with the increased independence from its owners. One aspect of this was to build up services for the members' companies. More emphasis was put on the service of the technical department that also took care of the implementation of new work methods and cost analysis. The technical department also took care of the implementation of a new salary system in the fish industry based on a bonus system. This meant great emphasis on work analysis, time measurements and work descriptions. Quality control was also a big part of the IFPC's operation during this time. There was also an expansion in other services

¹⁰⁹ Hannibalsson, Ó. & Einarsson, H..

¹¹⁰ Hannibalsson, Ó. & Einarsson, H.

¹¹¹ Hannibalsson, Ó. & Einarsson, H.

that IFPC provided for its members, leading to an increase in IFPC's operations. It is clear that IFPC was now much more than a marketing company, as it was meant to be, and it can be claimed that it served its members with almost all of their needs, including supplies for their production, consultancy for their business, and selling their products.

The strategy of IFPC and its owners during this time was clearly that all matters that would benefit the members companies would be done inside IFPC or other companies connected to IFPC. These companies included: Jöklar hf., which was a sea transportation company; Umbúðamiðstöðin hf., which produces boxes for fish fillets as well as other boxes that were used by the members of IFPC; and Tryggingarmiðstöðin hf., an insurance company that took care of insurance for the members of IFPC. Umbúðamiðstöðin and Jöklar were in joint ownership by IFPC and their members' companies but Tryggingarmiðstöðin was in a majority ownership by the members' companies of IFPC.

Another aspect of IFPC's operation during this period is the role of IFPC as an acting interest group for its members. This role focused mainly on taking care of its members' interests against the government in a highly regulated environment¹¹². Due to difficulties in the operation of the fish industry in 1966–68 and again in 1972–76, this role took a lot of the IFPC's managers, attention, as well as of managers of the PPCs. IFPC also played a big role in the pricing of the raw material that was decided by a price committee with an equal number of representatives from the fish industry and fishing sector. The government nominated a referee to judge the price so in practice the government more or less decided the price of raw material.

There were two main markets that IFPC was working on during this period. The main market was in the US, where IFPC sold its products through its subsidiary, Coldwater US. The second most important market was in Eastern Europe, mainly in the former Soviet Union. For a decade, these two markets took over 90% of the total production of IFPC members (see figure VI.1)¹¹³. The US market reached its peak around 1979 but after that the

¹¹² See the discussion in chapter II.3.

¹¹³ Hannibalsson, Ó. & Einarsson, H.

importance of the two main markets in Eastern Europe and the US declined and other markets such as Western Europe and Japan increased. Due to booking “6” in the agreement between EFTA and European Union, abbreviated EU (which became active in 1976) that lowered the import toll on fish product to EU countries from EFTA countries, the Western European market started to increase for IFPC. In the 1970s, IFPC sold around 75% of the total frozen fish exported from Iceland, and this portion reached its peak in 1976 when it was 77.4%¹¹⁴.

It is interesting to see how much emphasis was put on these two markets. Hence, the risk was very badly distributed. Partly this can be traced to high tariffs on fish products into the EU, as well as the extensions of the economic zone around Iceland. The extension of the economic zone around Iceland caused a dispute between Iceland and the EU. Hence, EU delayed the activation of booking “6” until the dispute had been resolved, and other import barriers were also put on fish from Iceland¹¹⁵. On the other hand, the strong position of Coldwater US during this period can explain why less emphasis was put on new markets. It is clear from the history of IFPC that Coldwater very much had independence from the other operations of IFPC and was in many cases the leading force of other developments. As one of managers of IFPC said,

“it can be said that Coldwater US was a state inside the state”¹¹⁶.

A similar was expressed by other interlocutors. An example of the strong position of Coldwater US is when IFPC wanted to change the name of its subsidiaries in the UK to Coldwater UK in 1980. Þorsteinn Gíslason, manager of Coldwater US, refused this and claimed that Coldwater US owned the name “Coldwater”. As a result, the name was not changed to Coldwater UK until 1996¹¹⁷.

¹¹⁴ Hjaltason, J., Einarsson, H. & Hannibalsson, Ó.

¹¹⁵ Hannibalsson, Ó. & Einarsson, H.

¹¹⁶ Interview with manager of IFPC, I-2.

¹¹⁷ Morgunblaðið 14. November 1996, interview with Agnar Friðriksson, General Manager of Coldwater UK.

Highlights of the operation of IFPC and its subsidiaries during this time included:

- 1962 Decision taken to stop operation of secondary plant in UK
- 1963 Coldwater US stopped commission sale of fish from IFPC members. Instead, Coldwater bought all the fish they sold for their own account.
- 1964 Umbúðamiðstöðin (packing company) established.
- 1965 Licence granted to build new secondary processing plant in Cambridge US.
- 1969 Coldwater established Royal Guard to operate fish and chips shops in US. The reasons were twofold. First to sell Icelandic fish and secondly to learn how to run shops like this to become better sellers. This operation was stopped in 1973-74 and the reason given was that it was negative to be in too much competition with their main buyers.
- 1969 Operation of Snax Ross reached its peak of operation with around thirty fish and chips shops. In 1983, the last fish and chip shop was sold.
- 1970 Coldwater US made an agreement with producers in Faroe Islands to sell their product in US. The Faroe Islands producers got the same terms as members of IFPC.
- 1972 Coldwater made sales agreement with Findus in Denmark to sell their products
- 1977 IFPC bought 39,9% share in Jöklar hf., which had previously been in ownership of the members' companies of IFPC. Later, in 1980, IFPC increased its share in Jöklar hf., to over 90%.
- 1978 New secondary processing plant started its operation in Boston US

Due to the growth of IFPC and increased emphasis on secondary processing in the US by Coldwater US, a conflict of interest became obvious. This was reflected in an annual meeting of IFPC in 1970 when Þorsteinn Gíslason, general manager of Coldwater, claimed that when "block" (a product that is mainly used for secondary processing) was produced as some kind of by-product of other fillet packing it would damage the quality of the production. He claimed also that elsewhere block was only produced from whole fillets rather than from just some parts of the fillets that were not used in other packing.¹¹⁸ It is obvious here that Þorsteinn was talking for the

¹¹⁸ Annual meeting of IFPC 1970, Hjaltason, J., Einarsson, H. & Hannibalsson, Ó.

interest of Coldwater as a secondary producer but not as a sales representative aiming at paying the highest price to producers and increasing the value of their production.

Constellation characterizes the operation of IFPC during this period, meaning that either IFPC or its owner took care of most of the needs of members' companies. Due to this constellation and centralisation of both knowledge and physical flow of supply and products through IFPC and its subsidiaries, it is clear that IFPC had every opportunity to gain much more power in this alliance than its members. An interesting example of the strategy during this time was a decision taken at an annual meeting of IFPC in 1968, when it was agreed that members' companies of IFPC were not allowed to buy boxes from companies other than Umbúðamiðstöðinni hf (a company owned by IFP and its members)¹¹⁹.

Equalization is the main concept in this period and one member had one vote on annual meetings, so, in theory no member's company could be in the position to have too much power. It is clear though that managers of the larger companies inside IFPC were in a leading position, mainly through the participation in the board of IFPC and its subsidiaries. Membership in the board meant that the managers were much closer to information and had easier access to both the staff of IFPC and information from the market.

VI.2.1.3 1980 - 1985 Strategy- and Generation Changes

The turning point for IFPC's operation was around 1980 when the market in the US declined and increased emphasis was put on markets in Western Europe by the establishment of marketing subsidiaries in Germany and plans for building secondary processing plant in the UK. Other markets grew stronger during this time such as Japan. It is clear that IFPC was changing its strategy during this time by starting to expand to other markets much more systematically than it had done before (see figure VI.1). Changes in this strategy can partly be traced to the result of the so called

¹¹⁹ Hannibalsson, Ó. & Einarsson, H.

“European committee” that worked inside IFPC in 1979, as well as the increased problems in the US market¹²⁰.

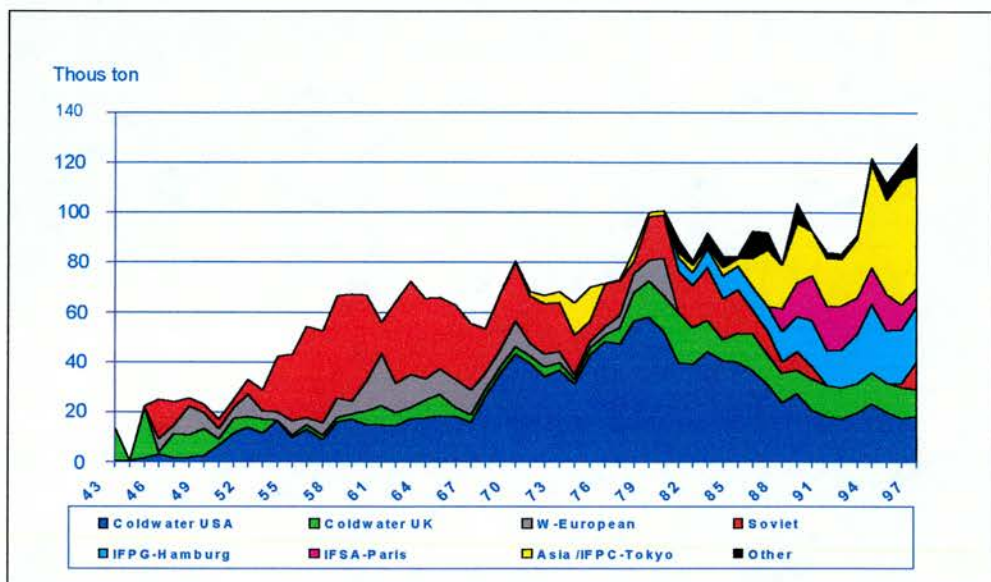


Figure VI.5 Total sale of SH split after market areas 1943-1997

Implementation of this new strategy started in 1980 when the board of IFPC agreed to start the preparation for building a secondary processing plant in Grimsby (UK) and changed the name from Snax Ross to Icelandic Freezing Plant Ltd. Production started at the plant in 1983. In 1981, IFPC established a marketing subsidiary in Hamburg (Germany). Other changes during this time included for example, when IFPC, in the autumn 1984, was allowed by its members to export and sell products from non-members. This is mainly due to pressure from owners of processing trawlers that were in many ways outside the PMCs and therefore did not have easy access to the markets. This is in many cases an interesting turning point in the history of IFPC. The fact that IFPC had started to sell for non-members indicate that IFPC was moving from being just for members towards becoming a more general sales and marketing company for fish products. Despite this turning point for IFPC it has to be remembered that Coldwater US had earlier, in 1970, made an agreement to take on the marketing of fish products from the Faroe Islands and, in 1972, for Findus in Denmark.

¹²⁰ Based on interview with former board members of IFPC.

At the annual meeting of IFPC in 1984, Jón Ingvarsson became the chairman of the board of IFPC. This was the starting point of a new generation of managers and board members of IFPC. The first and second generations had mostly left the industry and the third generation overtook operation of both PPCs as well as the PMCs¹²¹. These changes continued in 1986, when Eyjólfur Ísfeld Eyjólfsson resigned as general manager of IFPC and Friðrik Pálson was hired. Friðrik had previously been general manager of UIFP. In addition to this, new managers of finance and markets were hired to the IFPC¹²².

Highlights of the operation of IFPC and its subsidiaries during this period included:

- 1980 Snax Ross was renamed the Icelandic Freezing Plant Ltd., and preparation for building a secondary processing plant started
- 1981 IFPC established marketing subsidiaries in Hamburg (Germany).
- 1983 Production started in secondary processing plant in Grimsby (UK)
- 1984 In autumn 1984 IFPC was allowed to sell product from producers in Iceland that were non-members in the organisation.
- 1984 New general managers hired to Coldwater UK after Þorsteinn Gíslason resigned.
- 1988-86 Changes of president of IFPC, Eyjólfur Ísfeld resigns and Friðrik Pálsson hired.

The period of 1980 to 1985 was characterised by increased emphasis on globalisation by expanding the market operation to new markets as well as the decision to build a secondary processing plant in UK. This expansion of IFPC was both forward and backward in the value chain: Forward to new markets and backwards to get more producers (that is, non-members) to sell their products through IFPC.

It is obvious from the change of managers in Coldwater US and IFPC, and changes of the chairman of the board of IFPC, that there were some conflicts in the operation of IFPC during this time. After 1980, IFPC started to expand to new markets and in many ways implemented a new strategy. Hence, it is a question when relatively young men took over as chairman

¹²¹ Hannibalsson, Ó. & Einarsson, H.

and vice chairman of the board of IFPC in 1984 whether they have been pushing for getting younger men in as managers to implement the new strategy. At least it is clear, although unofficial, that the change of manager of IFPC and Coldwater was not as straightforward as it was meant to be¹²³. It is likely that both Þorsteinn and Eyjólfur were regarded to be too much solo players for the new board and the new generation of managers that were taking over in the PPCs and in the board of IFPC.

Very little changed concerning the relationship with the members during this time. Rather, it can be said that the ground for a new strategy was laid and the first steps taken to stop acting like an interest group. Service to the members kept on increasing with increased emphasis on technical and work methods development. In the law of IFPC act 7, the role of IFPC is made very clear:

“The board is responsible to take care of sale of member’s products and should in all matters of the sale make sure that the interest of members is taken care of. IFPC has the duties to pay all its members same price for the same production, equal of quality, which is exported and paid on period that members meeting or the board decide on.....”¹²⁴

In the same act, members are obliged to let IFPC take care of all their sale of frozen seafood. This act states clearly that IFPC is there to take care of its members’ interests in the sale of their export.

VI.2.1.4 1986 –1997 Globalisation and Structural Changes

As a result of the changes in the board and management team of IFPC, discussion started in 1986 of how IFPC could change their operation in accordance with the changes of the business environment during this time. These changes in the business environment included, for example, increased freedom in the economy, a foreseeable abolition of the duopoly of IFPC and SÍS/IS (Federation of Icelandic Co-operatives/Icelandic Seafood) on the sale of fish products to the US, and declining fish stock in the Icelandic sea.

¹²² Hjaltason, J., Einarsson, H. & Hannibalsson, Ó.; Hannibalsson, Ó. & Einarsson, H.

¹²³ Interviews with various managers of PPCs during the research.

¹²⁴ Hjaltason, J., Einarsson, H. & Hannibalsson, Ó., page 574.

Friðrik Pálsson, president of IFPC, continued this discussion at the annual meeting in 1987 when he talked about

“that IFPC should be sale organisation but the question was whether IFPC should be acting as an interest group for its members especially in the light of unclear boundaries between fishing and producing”¹²⁵.

Friðrik was referring to the fact that IFPC dominated one member in committee that decided the price of raw material for processing. In many cases the owners of the fishing vessels and the processing plant were the same. Hence, IFPC were representing processors against the owners of fishing vessels which were often the same company, causing conflict and confusion concerning on which side of the table members of IFPC were sitting. As a response to this discussion about the role of IFPC it was decided that IFPC would participate in the establishment of Samtök Atvinnurekanda í Sjávarútvegi, (Organisation of employers in the fish industry), abbreviated SAS, in the autumn 1987. The aim of SAS was to take over part of the operation of PMCs that included interest matters. By doing that IFPC more or less quit acting as an interest group for its members. Hence, the main aim now was to operate as a sales organisation for its members¹²⁶.

In November 1987, the Ministry of Trade gave six new exporters licences for exporting fish products to the US. This meant that the duopoly that IFPC and IS had on export to the US was abolished for good. IFPC reacted to this changes by claiming that due to limited competition between sales companies from Iceland they were the leading sales company on the US market. Because of this they were leading in price formation on the US markets and could get higher price than other competitors. Hence, they could return higher prices to the Icelandic producers¹²⁷. The abolition of the duopoly was just one of the milestones towards increasing competition and freedom in the market.

¹²⁵ Hannibalsson, Ó. & Einarsson, H.

¹²⁶ Hannibalsson, Ó. & Einarsson, H.

¹²⁷ Hannibalsson, Ó. & Einarsson, H.

It is interesting to see the efforts of Friðrik Pálsson, president of IFPC, to maintain the restrictions on competition in the marketing of fish from Iceland. At the annual meeting in 1990 he claimed that the old saying "*together we stand but divided we fall*" was still valid in the export of fish products from Iceland. He also claimed it was clear that the primary marketing companies were the only hope for the private enterprises in the fish industry. The primary processing companies were too small to be able to implement "*go it alone*" strategies in marketing of their products. If they would do that they would need to depend on foreign companies, which both now and in the future would be in a dominant position against the small Icelandic producers. Hence, it was only through companies' network or big companies that producers could maintain their independence against these foreign buyers¹²⁸.

At an annual meeting in 1988, major changes in the philosophy behind the organisation were agreed on. The main change was to abolish the one-member/one vote system. In the new system, 20% of the votes were distributed equally, 40% of the total votes were distributed in accordance to the value of export of each company through IFPC and the last 40% of the total votes were distributed to each company in accordance to its ownership in the equity fund of IFPC¹²⁹. Despite this, each company had a veto on agreement that was bound in the memorandum of association agreement, so theoretically, one company could block changes. This happened in 1990 when a change of this veto system was planned. These proposed changes meant that instead of requiring the agreement of all members for changes in the law that were bound in the memorandum of association agreement, agreement of 2/3 of the members was enough. One member did not agree to these changes and blocked them. Hence, this veto was kept unchanged until IFPC was changed into a limited liability company in 1997¹³⁰.

The constellation strategy of IFPC, which was to participate in all matters that were beneficial for its members inside IFPC, started to change after

¹²⁸ Friðriks Pálsonar speech on the annual meeting IFPC 1990

¹²⁹ Hjaltason, J., Einarsson, H. & Hannibalsson, Ó.

¹³⁰ Hjaltason, J., Einarsson, H. & Hannibalsson, Ó.

1990. The first step in that direction was the reduction and final abolition of the technical department over the years 1993 and 1994¹³¹. Changes of this strategy became more obvious in 1996 and 1997 when IFPC sold its share in Plastprent hf., and Umbúðamiðstöðinni hf. At the same time IFPC quit the sea transportation operation of Jöklar, which was terminated and changed into a holding company to take care of its investment in other companies. This clearly demonstrates the leading strategy during this time that is “*do well what we do best and let other take care of the rest*”¹³². This was a practical indication that IFPC was focusing on the international marketing the fish products. This is in accordance with trends in business operation during this time, to stick to the core business and let others do what is their core business¹³³.

In the period before 1995, IFPC had limited its vertical integration into production to foreign companies. In 1995, Icelandic Seafood h.f. (abbreviated IS), the main competitor of IFPC, bought around 30% share in one of the biggest producers, Vinnslustöðin hf., a member in IFPC. This meant that the marketing of its products would move from IFPC to IS. A similar situation arose concerning the biggest producers of IFPC, Útgerðafélag Akureyrar hf. (abbreviate ÚA). During this time, ÚA was in the majority owned by the town council of Akureyri. IS offered to move its headquarters to Akureyri if ÚA moved in its business. This ended in competition between these two companies about the business of ÚA. The result was that IFPC kept ÚA's business, but moved 1/3 of their headquarters to Akureyri.

IFPC had the strategy of not being vertically integrated into its members. In many ways, this competition reflected one of the main criticisms/weakness of IFPC and its form during this time: that is, it was too slow to react to such a situation. It also demonstrates that IFPC's ownership form and relationship with its members limited in many ways its ability to react

¹³¹ Hannibalsson, Ó. & Einarsson, H.

¹³² Hannibalsson, Ó. & Einarsson, H.

¹³³ See for example Hamel, G. & Prahalad, C. K., 1994.

quickly to changes¹³⁴. On the other hand, IS is a Limited Liability Company and was considered to be quicker to respond to changes. These differences were considered by many to be due to the difference of ownership form and strategy of the two companies.

In 1990, increased emphasis was put on the discussion about the ownership form of IFPC and whether it was necessary to change it into a limited liability form. In that year a future committee was established with the mission to make suggestions about the future role and ownership form of IFPC. This future committee concluded that IFPC should not change its ownership form into a limited liability form¹³⁵. Despite this, it was clear that from around 1990 the pressure on IFPC to change its ownership form would increase. This was due to factors such as:

- General changes of the business environment towards more freedom.
- Changes in the fishery management system meaning less quota leading to less supply from members in Iceland into the sale network and therefore increased pressure for fish products from other countries and companies.
- Changes in the production sector where companies (often family companies) were increasingly going on the open stock market.
- Producers were merging and getting bigger.
- Due to often-low profitability in the production sector, members' companies left IFPC to free some of their share in IFPC. Hence, IFPC had to pay their share out, according to the IFPC agreement in 10 years time. Members claimed that they did not get the market price for their share in IFPC.
- Competitors like IS were in a limited liability form. This gave them better access to increased capital as well as a quicker response times to changes.
- UIFP went through the ownership changes in 1993/94. Many of IFPC's members were also members in UIFP.

Members of IFPC agreed to change its ownership form into a closed limited company as of January 1, 1997. The final push for this change was probably the competition between IFPC and IS for the producers. To get a better view of the development of members of IFPC during this period, the number of members and the ownership is presented in table IV.4.

¹³⁴ Morgunblaðið 29/11 1996.

Year	Ownership of 10 biggest members of IFPC (%)	Ownership of 20 biggest members of IFPC (%)	Number of members of IFPC
1986	47.27	70.47	80
1990	56.94	81.45	57
1996	75.91	97.14	34

Table VI.4 Development of members and ownership in IFPC¹³⁶

From this table, it is clear that the number of members declined by more than half from 1986 to 1996. This happened at the same time that the total sale of IFPC doubled. This indicates that increased quantity comes from producers that are not members of IFPC, as can be seen from the fact that in 1997 IFPC had in its business 123 producers¹³⁷. In addition, the ownership of the biggest companies of IFPC increased greatly, indicating that the bigger companies were getting even bigger. If this development continued, it seemed clear that IFPC would end up in ownership of a few big companies.

Highlights of IFPC's operation during this time include:

- 1987 The virtual duopoly that IFPC and SÍS had on export to the US was abolished
- 1989 IFPC established marketing subsidiary in France: Icelandic Freezing Plants Eur. Ltd. in Paris.
- 1989 IFPC established a sales office in Japan, which in 1997 was changed into IFP Ltd. Japan, a marketing subsidiary owned by IFPC.
- 1993 The board of IFPC agreed to participate in the operation of a company in India to fish and produce tuna in cooperation with a domestic company.
- 1994 IFPC bought Sæmark hf., which was a fish exporting company that specialised in the export of fresh fish from Iceland. IFPC used this company to sell and buy fish from non-members of IFPC.
- 1994 IFPC bought 50% of Superior Salmon Express in Belgium. This company specializes in the marketing of fresh fish.
- 1994 IFPC bought all the shares in Icecon hf., whose main business was the export of knowledge about fishing and fish production. After IFPC's buy-out the main aim of its operation was to get new

¹³⁵ Hannibalsson, Ó. & Einarsson, H.

¹³⁶ Built on IFPC Annual reports, 1986, 1990 and 1996.

¹³⁷ Hlutfjárlysing IFPC 1998. (Analysis for stock bidding for IFPC 1998).

- business connections and products for IFPC and its subsidiaries to sell.
- 1995 IFPC moved 1/3 of its headquarters operation to Akureyri after war with its main competitor IS about the marketing products for ÚA Akureyri.
 - 1994 IFPC bought a 50% share in Faroe Seafood Ltd., which operated a secondary processing plant in Grimsby. In 1996 Faroe Seafood Ltd., and Icelandic Freezing Ltd., UK merged to become Coldwater Ltd., UK where IFPC owned 75% share against, 25% share ownership of the previous owner of Faroe Seafood Ltd.¹³⁸.
 - 1996 IFPC established a marketing subsidiary in Spain, Icelandic Iberia S.A.
 - 1996 Changes of IFPC ownership form from Co-operative to Limited liability.

The relationship between IFPC and its members during this time changed apparently more than during other periods. First came the abolishment of the total equality of each company, indicating that the companies with more export should have more to say than the smaller ones. Another change was the abolition of the constellation: that is, being a member of IFPC meant that you were part of a family, which provided you with all your needs. Members' companies moved their business increasingly to companies that were outside the family, for example insurers. This reflected the general trend in the business environment in Iceland during this time to look for the lowest price through bidding out their business.

Another indication of changes in this relationship came from the chairman of IFPC in an interview in 1991, where he declared that Coldwater US bought only 35% of its fish for its secondary processing plant from Iceland. He carried on by saying

*"...it was always clear that the secondary processing plant had to have independence from the producers in Iceland and be free to buy fish from the most convenient suppliers each time"*¹³⁹.

In the same way Agnar Friðriksson the general manager of Coldwater Seafood UK, said

¹³⁸ Built on IFPC Annual report 1996.

¹³⁹ Hjaltason, J., Einarsson, H. & Hannibalsson, Ó., page 15.

“...that the only duties they had was to make profit and sell the product from IFPC members on as high price as possible”.

He declared further that they had no commitment to buy fish from IFPC's members (Icelandic producers) for the secondary processing plant. In 1996, around 25% of the fish they used came from Iceland¹⁴⁰. It is clear from these statements that the strategy of IFPC was to operate secondary processing plants, which were independent from the sale of members' products and with profit. On the other hand, the operation of the sale of members' products was supposed to operate on a low margin with profits returned to members. The boundaries between these operations are often not very clear due to internal purchases for the secondary processing plants. Coldwater US purchased all the fish on its own account and then either used it for its plants or sold it on to other buyers. Producers in Iceland therefore did not know whether Coldwater US bought the fish for their own use or for further sale. This indicates a possible conflict of interest, where the profit aim of Coldwater could easily overcome the overall strategy of IFPC to return the profit to members. A similar situation was happening with other marketing subsidiaries: that is, they were increasingly purchasing the fish on their own account for further sale.

The changes of the relationship between IFPC and its members moved more from the *“one for all and all for one”* towards a more independent relationship. The formal power moved more to the bigger companies due to changes in the voting system. Despite this, some equalization was kept by the veto system, although that was possibly more symbolic than real. The operation of IFPC itself moved more to the markets, leaving IFPC more and more like a mother company with a more supportive operation rather than the basic sale itself.

In table IV.5 are figures from the operation of IFPC during this period. These figures are for the operation of the Consolidation (that is, IFPC and its subsidiaries). As can be seen from the figures the net sale of IFPC had increased from 1986 to 1996 by 93%. This increase can be traced to the sale

¹⁴⁰ Morgunblaðið 14. November 1996. Interview with Agnar Friðriksson, general manger of Coldwater UK.

of products of non-members, which had greatly increased during this period. In 1996, 13% of the total sale came from foreign producers that sold their products through IFPC or its subsidiaries¹⁴¹. IFPC had around 43% share of the total value of frozen fish export from Iceland in 1996.

Year	Net sale in ISK '000	Return on operation revenue	Equity ratio	Return on equity in %
1986	12,802,646	0.63%	26.8%	6.6%
1990	16,454,865	1.84%	19.9%	18.7%
1996	24,744,136	2.9%	23.0%	19.3%

Table VI.5 Key operational and financial figures 1986 - 1996¹⁴².

VI.2.1.5 1997 – 1999 Independence

The ownership change of IFPC was followed with a new definition of the role of IFPC, was as follows:¹⁴³

- IFPC is a global sales and marketing company for frozen fish products.
- IFPC's main task is to provide services for production, sales, marketing, development and quality control of seafood products. This service is provided to producers in Iceland and overseas.
- Another objective is to operate subsidiaries outside Iceland, both for marketing products from suppliers and processing them further by operating fish processing plants

This role is defined in the mission of IFPC as "*IFPC operates subsidiaries overseas to ensure marketing of products, and to process seafood products. In order to ensure its market position and growth, IFPC makes production and sale agreements with Icelandic as well as overseas parties and invests in production and marketing companies. The company shall yield a normal return on the capital invested in it at any time.*"¹⁴⁴" For the first time in over fifty years' history, IFPC's aim was to make profit for its owners and not to pay it back in lower commission. IFPC had also changed its strategy and allowed the option of vertical integration by buying shares in producers in both Iceland and abroad.

¹⁴¹ Hlutfjárýsing IFPC, page 36. (Analysis for stock bidding for IFPC).

¹⁴² Annual report 1986, 1990 and 1990. In this table revenue is taken from the coalition of IFPC the mother company and subsidiaries

¹⁴³ Information from, <http://www.icelandic.is/>.

The chairman of IFPC during this time declared in an interview that with the changes of IFPC into a Limited Liability Company, it would have to change its relationship with its former members. This new relationship would build on business relationships, and the sociological relationship and view would be abolished¹⁴⁵. After the ownership change, companies inside IFPC were no longer bound to hand over all the frozen products. Instead, individual companies made a sales contract (service agreement) for part, or all, of their products, which was terminable from each side with six-months notice. In this service agreement, IFPC is undertaking to monitor the products in all parts of the process, from production to delivery of the product to the final buyers. This entailed, for example, that IFPC consults the producers about what products are suitable to produce, about the condition of markets, and that it also takes care of all transportation and documentation for the export. In addition to this, producers were now under the control of the quality department of IFPC, and had to fulfil the standards that IFPC now makes on each product it sells. Producers can also make contracts with IFPC for supplies of various operational goods, in particular packing. This means that producers are no longer bound to buy their packing from IFPC and can buy from elsewhere as long as it fulfils the quality standards of IFPC¹⁴⁶. In addition, IFPC operates an R&D department, which aims to increase the value creation of the production as well as meet the needs of the buyers and consumers of the products¹⁴⁷.

Producers that make a service agreement with IFPC get services from IFPC with the aim of providing the producers with the highest price as possible as well as information about the market. Sæmark h.f., the trading subsidiary of IFPC, then takes care of other producers that want to trade on the free market. Sæmark h.f. either buys the product for further sale or sell it in commission sale. Sæmark h.f. does not have the same obligation to the producers about information or other services as does IFPC h.f. By this IFPC claims that they can keep the operation of IFPC producers oriented so

¹⁴⁴ Mission Statement of IFPC taken from the <http://www.icelandic.is>.

¹⁴⁵ Hannibalsson, Ó. & Einarsson, H.

¹⁴⁶ Built on information from <http://www.icelandic.is>.

that they can return as high price for the products as possible and provide producers with more service than would otherwise be possible.

Highlights of IFPC's operation during this time include:

- 1997 IFPC established a marketing and purchase subsidiary in Russia. (IFPC Russia) In 1997 IFPC also bought a fish wholesale company in Russia, which sells considerable quantities in and around Moscow, and established a holding company, Navenor Holdings Ltd., to run it.
- 1997 IFPC established a marketing and purchase office in China
- 1997 IFPC established a subsidiary in Norway (IFP Norway A.S.), which aims at providing products for IFPC's sale and production system worldwide.
- 1997 At a shareholders meeting in 1997 it was decided to lift all restrictions on the sale of shares in IFPC and the company applied for registration on the Iceland Stock Exchange.
- 1998 The operation of Coldwater UK was split up into two companies. On the one hand is Coldwater Seafood UK LTD, which takes care of the operation of the two secondary processing plants and sale of its product. On the other hand is the sales company IFPC UK that takes care of selling products of companies that sell through IFPC.
- 1998 In the beginning of 1998 the Iceland Stock Exchange approved trading of IFPC shares on its main stock market.

After the ownership changes of IFPC the nature of the alliances changed into alliances between IFPC and individual companies rather than joint venture (alliances) between the producers to market their own product. This change did not happen overnight; it was rather a development over the past decade, which was finally confirmed formally and legally by the ownership change. Now each company had to deal directly with IFPC, and a new force in the network had emerged: that is, the shareholders. The majority of the shares is still in the hand of producers, but some producers used the opportunity to sell their share and use the money in their own company. At the end of 1998 the ten biggest shareholders owned 75.79% of the total share and were all former members of IFPC and producers. The twenty biggest shareholders owned 92.67% of the total share, and six of them were banks or other investors that were not directly involved in production of

¹⁴⁷ Hlutfjárðing IFPC, page 38. (Analysis for stock bidding for IFPC).

fish. The total number of shareholders on 30th December 1998 was 302¹⁴⁸. Although the majority of shares is in the ownership of producers, it is clear that there is a new emphasis on the shareholders' value in IFPC's operation. Therefore, we can talk about three main forces: the IFPC, producers and shareholders.

One of the obvious changes in IFPC's strategy is the vertical integration into the production sector. In September 1997 IFPC owned share in only one producer (a 10% share in ÚA h.f.) but Jöklar, the Handling subsidiary of SH, owned share in seven producers. In none of the companies are IFPC or its subsidiaries in dominant positions.

In table VI.6, key figures from the operation of the Coalition of IFPC for the years 1997 and 1998 are presented.

Year	Net sale in ISK '000	Return on operation revenue	Equity ration	Return on equity	Number of staff	
					Icel.	Abroad
1997	28,484	0.97%	17.3%	8.52%	100	1169
1998	16,454	1.84%	19.9%	6.82%	N/A	N/A

Table VI.6 Key operational and financial figures 1997 - 1998¹⁴⁹.

VI.2.1.6 1999 - ?

A new turning point for IFPC came during the annual meeting in March 1999 for the year 1998. Then, Róbert Guðfinnsson, chairman of Þormóður Ramma hf., and the biggest shareholder in IFPC, was elected as chairman of the IFPC board in competition with the sitting chairman. Róbert claimed that his candidature as chairman was due to an increased dissatisfaction with IFPC's operation. Róbert's election was guaranteed after he and others around him had increased their share in IFPC the night before the annual meeting¹⁵⁰. Soon after the annual meeting, Friðrik Pálsson, president of IFPC, resigned as president and a new president was hired. The main criticism of IFPC was that the centralisation of its operation that was not adding value for producers or for IFPC. The new board and president have

¹⁴⁸ Hlutafjárlysing IFPC, page 9. (Analysis for stock bidding for IFPC).

¹⁴⁹ IFPC Annual reports 1997 and 1998. In this table revenue is taken from the coalition of IFPC the mother company and subsidiaries.

¹⁵⁰ Frjáls Verslun 3. tbl., 61. árg., 1999.

not presented much about the planned changes, but from interviews with them in the media and an interview with Róbert Guðfinnsson, the main changes concerning this research seem to be the following.

- Increase the formal authority of president of IFPC by making him chairman of board of all IFPC's subsidiaries.
- Abolish the big producer's board over each subsidiary.
- Make each subsidiary more independent to make contracts and buy direct from producers.
- Move activities to producers and subsidiaries from IFPC MC to decrease centralisation in the process. This was done for example by abolishing the R&D department of IFPC MC.
- Move IFPC's sale system closer to the consumer.

The aim of these changes is to decrease centralisation to make the network more effective. It seems obvious as well that contract between IFPC and producers will no longer exist; rather, producers will make contracts with each subsidiary¹⁵¹. These changes are meant to bring more freedom in the network and ensure that producers will have chosen how and through whom they sell. It is clear as well that the IFPC sales network will be evaluated on a much more competitive base against its competitors. One aspect of these changes is that for the first time IFPC defines its role or vision to be an "*international marketing company for fish products*" and not a service company for producers¹⁵². As a confirmation of this change, IFPC abolished Jöklar hf., the holding company, and sold almost all its shares in other companies. In accordance to this IFPC sold Sæmark h.f., and has cut its business down to frozen fish as its core business. Despite this IFPC still focuses on good cooperation with producers, but not as only a service company for them.

¹⁵¹ Interview with Róbert Guðfinnsson 20.05.99.

¹⁵² Interview with Róbert Guðfinnsson 20.05.99.

VI.2.2 Analysis of the IFPC Case

VI.2.2.1 Nature and forms of the alliance

The nature of the alliance between IFPC and producers has changed a lot during the operation time of IFPC. From analyses of the history of IFPC, four basic shapes of the alliance have appeared.

First is the period from 1942 to 1962 where the form is clearly a joint venture between producers, and IFPC took care of the marketing activities of the producers. In many ways this form has many of the characteristics of a parent-child relationship; the parents (the producers) have the formal power and authority in the alliance, and the child (IFPC) suffered from lack of independence and opportunity to mature. The difference from a normal or traditional joint venture is the number of parents: over twenty companies instead of two companies forming the joint venture. In many ways this could indicate that the child would gain more power over time due to high numbers of parents and the central position of the child. In this case, it is clear that management of the alliance is in the hands of the chairman and the board of the IFPC, where all participants in the board are managers of PPCs. Hence, the alliance was more or less hand controlled by the board where the main strategy seemed to be based on shared benefits for the PPCs. The main philosophy of the alliance during this time was based on equalisation that is, *“one for all and all for one”* (see figure VI.6).

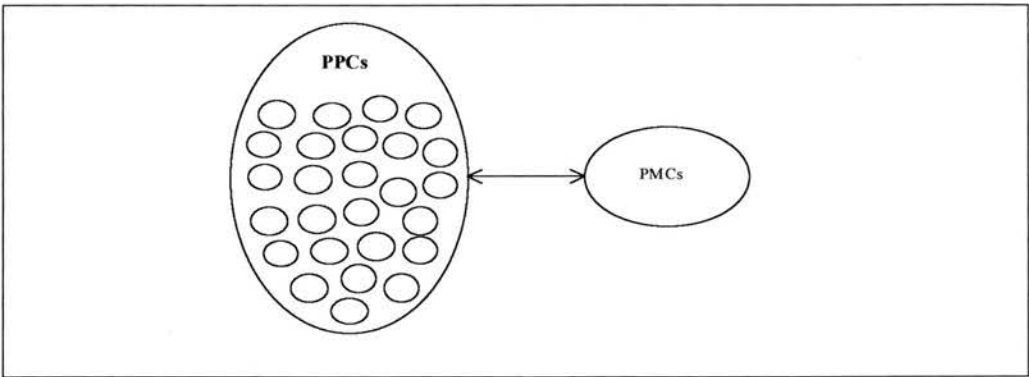


Figure VI.6 Form of the IFPC alliances 1942 - 1962

Although each individual company has its own relationship with IFPC the producers were all treated in the same way and looked at as a single group.

In the end of this period IFPC was close to collapse due to factors such as too high dependency of its members, lack of independence to take care of its own matters and lack of leadership and strategy.

The second period was from 1962 to 1996 when IFPC gained more independence from the producers. Then the alliances still had the main characteristics of a joint venture between the producers because IFPC treated them all in the same way and equalization was still one of the main aims during this time. Other characteristic during this period is constellation around IFPC and its operation. This was reflected in the fact that IFPC participated in almost all parts of the process of production and selling of the products, and related businesses (see figure VI.7).

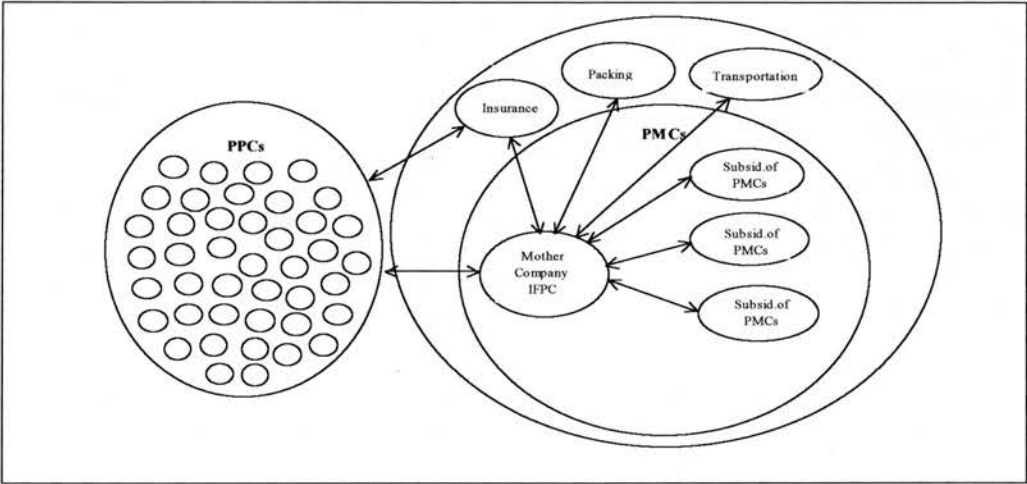


Figure VI.7 Form of IFPC alliances 1963 - 1996

During this time, IFPC certainly gained much more power and authority than each individual producer had in controlling the constellation. This form starts to break down in 1986 when IFPC started to take in producers that were non-members. Then members had their capital bound in IFPC while other could use the sale network and service without binding capital in IFPC. After 1990 the relationship moved more clearly from the constellation and treating the members as one single group into more individual relationships. This was due to, for example, increased direct connection between producers and subsidiaries, and also the fact that producers were increasingly connected directly to sales contracts. Despite this, the formal structure of the alliances was the same, although there were

clear signs that participant companies were increasingly ignoring this structure.

The third period is from 1997 to 1999 when IFPC was changed into a Limited Liability Company. Then the alliance formally changed from being a joint venture between producers to becoming individual alliances between IFPC and each producer based on mutual contract (see figure VI.8). In addition to this, it is clear that the formal communication structure (through the central firm IFPC) is increasingly broken by direct communication from producers to the marketing subsidiaries of IFPC.

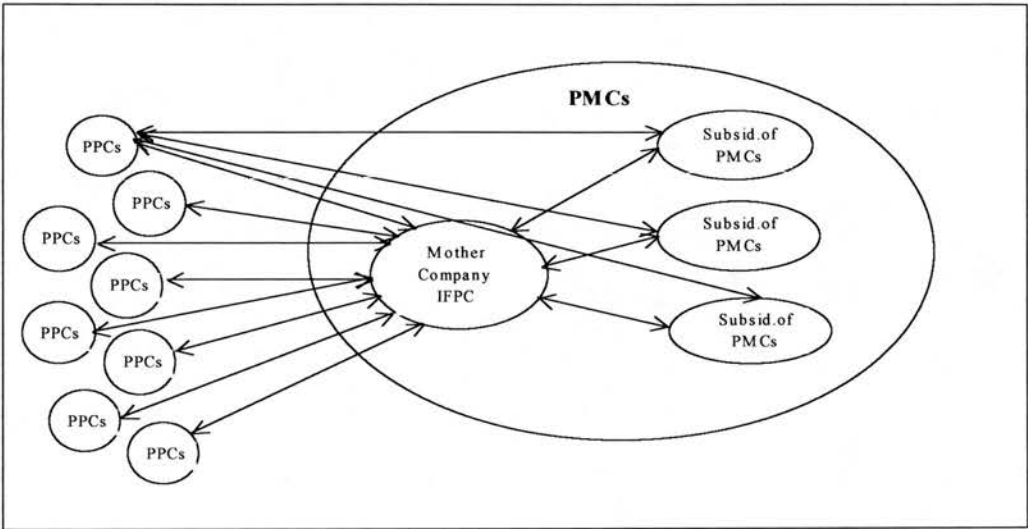


Figure VI.8 Form of IFPC alliances 1997 - 1999

Some would maintain that there was no alliance after this time; the relationship was built on a pure business relationship. There are signs indicating that IFPC is trying to maintain the relationship with its producers on a close alliance base. These indications are, for example, the close relationship of the R&D department with the producers, and the close relationship and service that IFPC is offering to producers. It is clear, though, that many of the producers feared how this would develop after the ownership changes of IFCP. One manager of a PPC that was a member of IFPC declared in an interview with Morgunblaðið (The Morning paper):

"Before the change of IFPC, it had been the sale department of the producers. If the company will be independent limited liability company then the marketing part will be cut from the producers."¹⁵³

¹⁵³ Morgunblaðið 1. May 1996. Interview with Finnþóga Jónsson manager of SÍN.

He also claims that this would push the producers to sell their product themselves, with a much worse result. It is clear that before the ownership changes there was some uncertainty of what would happen to the relationship between IFPC and the producers. Clearly, the relationship moved towards a business relationship, as a manager of IFPC claimed:

“IFPC the Mother Company aimed to have its operation “producers aimed”, with close relationship with producers that have service agreement with IFPC..... Due to the profit aim, it is clear that IFPC will need to make profit of the business with companies with service agreement. In the same way it is clear that IFPC has other opportunities to make profit in the constellation and if we manage to do that we can keep the margin from the business with the producers at a minimum” ¹⁵⁴

This clearly indicates that IFPC’s strategy is to maintain a close relationship with its producers. The other opportunities to make profit are, for example, through IFPC’s subsidiaries such as Sæmark, secondary processing plants and the sale of products from other producers.

The fourth and last period is the planned change in the operation of IFPC in the Spring of 1999. These changes will move the IFPC Mother Company out of the direct process between producers and the marketing subsidiaries (see figure VI.9).

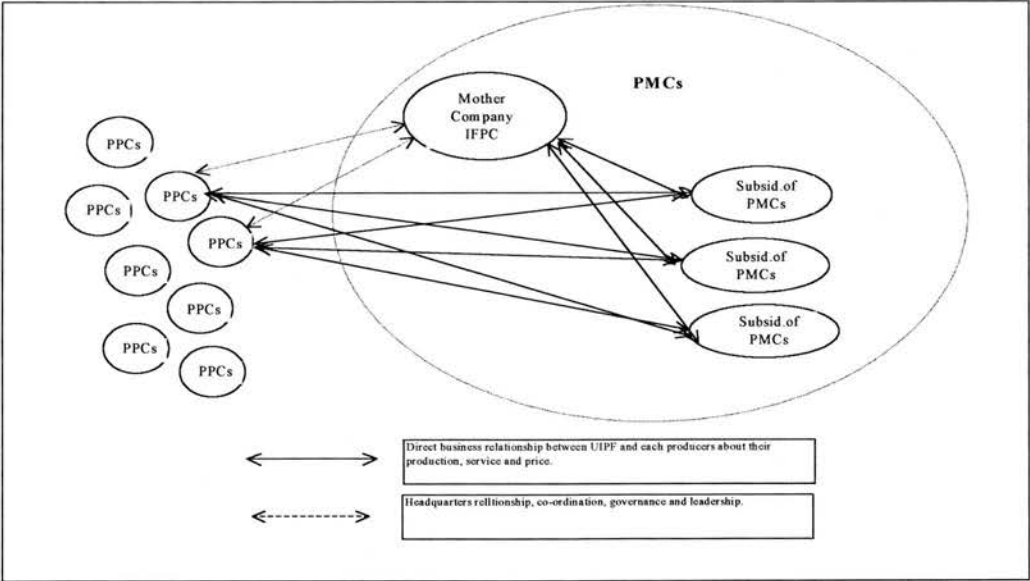


Figure VI.9 Form of IFPC alliances 1999 - ?

¹⁵⁴ Interview with manager of IFPC, I-3.

These changes are in many ways confirmation of the increased tendency of producers to have direct contact to the markets instead of having the middle step in the form of contacting IFPC's Mother Company. Producers have also become bigger and increasingly emphasized on building up market knowledge inside their own company instead of relying completely on IFPC. In addition to this producers have also taken on other activities that traditionally were based in IFPC, as for example R & D. This is in accordance with the strategy of IFPC that producers themselves take care of these activities with assistance from IFPC. This will also affect the form of the relationship because producers will now no longer make a contract with IFPC as a whole but instead have the option of making long-term contracts with each of the marketing subsidiaries. This will make the strategic alliances direct between these actors in the network. At the same time, this will increase the trading part of IFPC, which means that more and more of the business will focus on pure buyer and seller relationships.

VI.2.2.1.1 Nature of the alliance

It took members of IFPC a long time to take the last step in changing the IFPC into limited liability, which reflects the fact that members had some doubts about how it would affect the relationship between the PPCs and IFPC. The quotation as "*IFPC was the market division of producers*"¹⁵⁵ raises the question of the nature of the relationship between PPCs and IFPC. To analyse the nature of the relationship it is helpful to look at the basic model of the network perspective put forward of Hakansson H and Johanson J¹⁵⁶. That model consisted of three main factors: that is actors, activities and resources.

In the relationship between IFPC and its members, there are three main types of actors involved: producers, IFPC and its subsidiaries. The producers are then split up into individual producers, whose numbers have varied from around thirty to ninety. In table VI.7, the main factors involved in the network are summarised. These factors have been more or less the same over the last two to three decades. It is, however, obvious that there is

¹⁵⁵ Interview with a manager of IFPC Mother Company, I-4.

¹⁵⁶ Hakansson, H. & Johanson, J., 1992 .

not as sharp a difference between each type of actor as there was in the early stage of the network. Table VI.7 presents the different activities and resources depending on the actors in the IFPC network.

		PPCs	IFPC	IFPC subsidiaries
Activities	Top level	Managerial, strategy, financial matters	Managerial, strategy, financials matters	Marketing connection with IFPC and producers
	Middle level	Day to day activities and information gathering in activities sale, quality and shipment	Co-ordination, connection with marketing subsidiaries and producers	Sale of fish, information collection and connection with marketing division of IFPC
Resources		Fish stock Knowledge in fishing and primary processing	Brand names Overview over the whole process Marketing information Marketing connection	Brand names Marketing connection Marketing information

Table VI.7 Actors, Activities and Resources

The importance of each actor in the network has changed over the operation time. Before 1986 the IFPC was in a key position in the network due to the large percentage of the total sale, which went through them, as well as both the physical flow of products and the flow of information being controlled through the IFPC Mother Company, (abbreviated IFPC, MC). During this time direct contact between producers and marketing subsidiaries was not appreciated by IFPC¹⁵⁷. Coldwater US was also an important actor during this time, but as the importance of other markets increased the role of Coldwater US declined. In a similar way, after 1986 the actual sale was moved from IFPC, MC to the marketing subsidiaries and the importance of IFPC, MC declined. In addition, other supportive activities have been moved from IFPC, MC to the free market, leaving IFPC headquarters in the middle of the process from production to markets without an obvious purpose in the day-to-day relationship apart from coordinating the process.

VI.2.2.1.1 Stakeholders

One aspect of analysing actors and relationships in the alliance involves consideration of the stakeholders. Many of the stakeholders are not directly linked to the daily activities of the network but could influence the nature of

¹⁵⁷ Based on interviews with present and former managers of PPCs and IFPC.

the alliance and how it is operated. In the network perspective stakeholders are usually not mentioned, leading to a lack of depth in the analyses.

Before 1997, producers were almost the only stakeholders in IFPC. They were also in a leading position in governing the IFPC, and therefore the whole network, by having all members in the board of IFPC and its subsidiaries. After 1997 this changed and shareholders came in as strong stakeholders. Still, in the beginning of 1999 producers are the biggest shareholders, but it is clear from discussion in the media that shareholders and their values are increasingly putting pressure on IFPC and the whole network. This could be seen before the annual meeting for the year 1998 when Róbert Guðfinnsson, a manager of a PPC, which was the biggest owner in IFPC, was running for chairman of the board against the sitting chairman. Róbert said in the newspaper that:

*“.....as an example of IFPC status now, little or none request is for the share in IFPC....”*¹⁵⁸

In a TV interview, he claimed the following

*“I have got clear message from the stock market that something needs to be done about IFPC status”*¹⁵⁹.

Clearly, this demonstrates the new pressure or force on IFPC and the network from shareholders. Although producers are still the biggest shareholders in IFPC, they increasingly demand profit and return of their investment instead of just a high price and service. At the same time that producers demand profits they also demand the highest price, which can lead to a paradox in the operation of IFPC. Hence, it can be difficult to fulfil the aims of all stakeholders in the network.

VI.2.2.1.1.2 Dependency of actors in the alliance

Dependency on products is the most obvious dependency between actors in the IFPC alliance. In the beginning of the alliance IFPC was completely dependent on products from its members. This did not change until around 1970 when Coldwater US made an agreement to sell products from

¹⁵⁸ Morgunblaðið 06.06.99. Interview with Róbert Guðfinnsson, manager of Þormóður-rammi.

¹⁵⁹ Interview on Channel 2 (Stöð 2) 07.03.99 with Róbert Guðfinnsson, manager of Þormóður-rammi.

companies in the Faroe Islands and Denmark. Before that, Coldwater US had started to buy fish for its secondary processing plants from producers other than IFPC members. During this time the (seventies and eighties) the US market was the most important market for IFPC, putting Coldwater US in a powerful situation. Due to this, it is clear that the IFPC constellation was breaking the complete dependency on its members. However, IFPC itself did not start to sell products from non-members until 1984¹⁶⁰. In 1997, 16% of the total turnover of IFPC was due to business with foreign companies, while around 25-30% of the fish for the secondary processing plants was from Iceland¹⁶¹.

On the other hand producers had to depend on IFPC to sell their products. According to the agreements of IFPC, members were not allowed to sell themselves or through other companies. This duty to hand over frozen products was not abolished until IFPC was changed into a limited liability company in 1997. After the ownership change of IFPC producers could sell through other companies, except the products that they had made a sales contract with IFPC to sell¹⁶². Theoretically speaking this was the first time that members' companies of IFPC could evaluate on a competitive basis options for the sale of frozen products without abolishing membership in IFPC¹⁶³.

Producers have had to depend on IFPC for information about the market. With improved communication and IT, producers are increasingly contacting the market directly. These contacts are mainly made with the marketing subsidiaries of IFPC. However, general information about markets in the form of statistics and trends are much more available now than two or three decades ago. Hence, producers were more or less completely dependent on IFPC for information and knowledge of the markets until 1997. It is obvious, though, that before that time producers

¹⁶⁰ Hannibalsson, Ó. & Einarsson, H.

¹⁶¹ IFPC Annual report 1997.

¹⁶² It is though common knowledge that many producers broke this duty by selling themselves or through other companies.

¹⁶³ This is relevant for frozen products. Many members' companies were also in some other products such as salting or drying, or could choose to sell through UIFP or other companies. In that case, they could of course evaluate options between different processing methods on a competitive basis.

placed much more emphasis on building up marketing knowledge inside their companies. In addition, from 1986 IFPC did not block, as obviously as before, direct communication between producers and the marketing subsidiaries, which makes this dependency less obvious.

Although IFPC had broken the dependency on products from its members' companies, they had to depend completely on its members for formal authority until 1997 when the ownership form was changed. This is due to the ownership form of IFPC and the fact that IFPC was not meant to make profit. Hence, IFPC had to get formal approval from members to take on larger financial commitments as well as any major changes on its operation. Allowing IFPC to build up a fund inside the company, although that fund was under the ownership of its members, decreased this dependency.

One aspect of the dependency of actors in the network was the existence of exit barriers on members to leave IFPC. These barriers were in the forms of time limitation and payback methods and time of member ownership share in IFPC. The time limits of leaving IFPC were at least one year. Members had to give one-year's notice that they planned to leave IFPC. Then the secession would be valid the second New Year from the time it was notified to IFPC. Then, when members left IFPC, they got their ownership paid back through certain payback methods, which calculated their ownership in IFPC according to the booking value of their share in the ownership fund. It is clear that the capital that members were paid was in no accordance with the "real value" of IFPC, and furthermore payment was spread over 10 years. This was clearly done to keep the network together, as one manager of IFPC said:

*"It is clear that the methods of payment when members left was done in accordance to one-site method according to IFPC law."*¹⁶⁴

Hence, this acted as a barrier to leaving, knowing that you would not get paid back the real value of your share. These exit barriers, in addition to the fact that members had to sell all their frozen products through IFPC, made the alliance appear in some way as enforcement to the producers. This was

¹⁶⁴ Interview with managers of IFPC, I-5.

reflected in an interview with a manager of a PPC in IFPC membership, when he was asked about the ownership changes of IFPC in 1997:

“Alliances built on enforcement are not likely to survive in modern business environment”¹⁶⁵.

In a similar way, an example of one of IFPC’s subsidiaries claimed the following:

“For too long time the alliances have been kept together for other reasons than IFPC is the best choice for the producers. Exit barriers and ownership form had been used above the competition to be the best.”¹⁶⁶.

It is clear that many producers saw the dependency as an enforcement to the membership where they could not choose ways of sell their products on a competitive basis. IFPC and its subsidiaries had gained much more independence from its members than members had from IFPC. On the other hand it was not until 1997, when the ownership form of IFPC changed, that members’ companies gained similar independence and the opportunity to choose sale methods on a competitive basis. This, in many ways, brings competition much more into the alliances. Hence, it is claimed here that it is not until after 1997 that there is some balance in the dependency between actors in the alliances. Key to this are the freedom to choose and competition. This is both for producers to choose marketing methods and for IFPC in choosing producers, but one aspect of the dependency is the commitment that IFPC has had to its members. After the ownership change, these commitments are much clearer and are included in IFPC’s service agreement with the producer.

VI.2.2.1.2 Conflict of interest

It can be difficult to avoid conflict of interest in networks such as IFPC; as Axelsson claims, the three factors actors, activities and resources are closely connected and can cause conflict and power struggle in companies’ relationships because *“actors in different levels, controlling different resources and being involved in different activities may differ in their*

¹⁶⁵ Morgunblaðið 1. May 1996. Interview with Brynjólf Bjarnason, manager of Grandi.

¹⁶⁶ Interview with an employer of IFPC subsidiary, I-15.

intentions and perceptions....”¹⁶⁷. In addition to actors in the network are stakeholders, whose objectives are often not in harmony with the day-to-day activities and aims of the actors in the network. According to Axelsson, conflicts are mainly associated with the actors in the network and their control over activities and resources. Conflicts between activities can, for example, be between the sales method (that is, commission sales) versus purchase of the product, as well as primary processing versus secondary processing. Conflicts between sale methods are one of the oldest conflicts inside IFPC. This can be traced back to when Coldwater US started to buy all products from Iceland for further sale. Producers in Iceland have often suspected them of buying the product at a low price, then stocking the products and selling them when the price went up again¹⁶⁸.

Due to increased buying by the marketing subsidiaries and the change of strategy of IFPC (that is to be profitable), it is clear that there is a danger of increased conflict between the producers, that want as high price as possible, and the IFPC that wants profit on its operation. This is obvious concerning the buying by secondary processing plants of their supply. In those cases, the transparency of the sale is not clear, where the overall aim of IFPC was to return as high a price to producers as possible. This is even more obvious after the ownership change, when IFPC is clearly now meant to make a profit as well as return as high a price to producers as possible. Hence, this introduces the potential for conflicts in the strategy, which can be difficult to harmonies in order to fulfil the aims of all actors and stakeholders.

The conflict between buying or selling the products in commission sale is not the only conflict between the operations of secondary processing versus selling product from primary processing companies in Iceland. When managers of IFPC and its subsidiaries were asked about conflicts between operating secondary processing and selling products for primary processing they, in most cases, admitted that there was a clear conflict of interest between these factors, as can be seen from following quotations:

¹⁶⁷ Axelsson, B., page 199.

¹⁶⁸ Based on interviews with former present and former managers of PPCs.

“It is clear that operation of secondary processing can lead to other aims than returning highest price and value adding back home”¹⁶⁹

“Operation of secondary processing plant demands that the emphasis on value adding is in the secondary plant and not necessarily back home with the producers. This also causes that information is often not necessarily returned home. So there is clearly conflict between these two operation”¹⁷⁰.

“...IFPC evaluated that it was causing trouble to have the same company selling products from producers in Iceland and product from the secondary processing plant using the same channel. The development has been in that way that inside IFPC are producers that are capable of breeding fish in Iceland. They have increasingly started to ask themselves whether it is likely that I can sell my product through company that itself is in breeding fish. Coldwater UK must think about their own matters and that is not necessarily in the best interest of producers”¹⁷¹.

“The secondary processing plant has a bit special status but it is clear that it would be problematic for us if we (in Iceland) would have to stock products in Iceland while the secondary plants would be buying fish from Norway. Then we would be breaking this agreement with producers. It has to be admitted that conflicts rise in these matters but they have been solved in good manners and that are conflicts that are quite normal and we need to think about the production and they need to think about themselves and then we find some agreement. The main issue is that we have a process to find some solution”¹⁷².

In a similar way, producers claimed that there were clear conflicts between these two parts. What is most obvious are comments about the lack of returning information from the markets. This information is vital for building up knowledge for further production and value adding in the production in Iceland. An example of this can be taken from a manager in a production company that was planning on going into secondary processing:

“We needed tools to draw the information from the IFPC subsidiaries about markets and technique. It is clear that the staff there was blocking information to us and they were not very happy about what we were planning to do. It is my conclusion that secondary processing and selling products from producers in Iceland does not fit together”¹⁷³.

¹⁶⁹ Interview with a manager of IFPC subsidiary I-1.

¹⁷⁰ Interview with a manager of IFPC subsidiaries, I-15.

¹⁷¹ Interview with a manager of IFPC subsidiary, I-17.

¹⁷² Interview with a manager of IFPC, I-4.

¹⁷³ Interview with former producer manager in PPC, I-31.

In a similar way an employer of an IFPC subsidiary claimed:

“IFPC needs to make profit on their capital bound in the secondary processing plants abroad so it is clear they put emphasis on doing that on the account of the further development in Iceland. Hence the operation of secondary processing plant can be seen as barriers on further development and processing in Iceland”¹⁷⁴.

This touches on one of the central issues in a network like IFPC, that is, the value creation in the network. This mixture, that is, the operation of a marketing network with the aim of returning the highest price to producers on the one hand, and the operation of secondary processing itself on the other hand, leaves IFPC with a paradox about value creation in this value chain. Where is the emphasis on value creation and value adding in Iceland: the producers or the secondary plants? The establishment of the secondary processing plants were well justified at the time they were established due to factors such as import barriers in the countries that would have made secondary processing and value creation in Iceland difficult. Other factors also affected this development as capability of producers in Iceland and the unstable economics in Iceland over a long period¹⁷⁵. This should not have been a barrier to further development in this field in Iceland in the last 5-10 years. Adding to this picture the decreased fish stock for the last 10–15 years means that producers often had difficulties in increasing their value creation by just increasing fishing as they often did before. Hence, the question arises whether the conflict of interests has influenced further development in this field in Iceland. Almost all interlocutors that stood outside IFPC claimed that the answer to this was “yes”, it had been blocking this development in Iceland; as one former product manager claimed:

“It was always taboo to talk about breeding fish in Iceland. It was claimed by IFPC to be too expensive to transfer the bread to Iceland, the product would be damaged in transportation, the distance from the markets was too long, the equipment too expensive and the production too complicated etc, etc....”¹⁷⁶

¹⁷⁴ Interview with an employer of IFPC subsidiary, I-15.

¹⁷⁵ See for example the discussion about the economic status in Iceland in chapter III.

¹⁷⁶ Interview with former producer manager in PPC, I-13.

However, this has been looked at in the light of the import barriers that existed on processed fish until 1986 in the EC and transportation that was mainly built on filling whole ship before the containers became dominant. This meant that the distance from the market was a big issue, but today, with increased frequency and smaller portions, in container, this is not the case. At the same time, it is also clear that producers in Iceland were in many cases not able to enter into further development of secondary processing, as illustrated by the following quote:

*"It is only recently that producers in Iceland have been capable of going into further processing, both due to knowledge in simple factors like language and then size and access to capital..."*¹⁷⁷

On the other hand, when a manager of IFPC was asked about this he pointed out that:

*"I do not think that it has been the case that our operation of secondary processing plants on two markets, US and UK has blocked this development in Iceland. There are big marketing areas for breaded fish and food where such food is a big part of the retail food there, as in France, Germany and a lot of the Scandinavian countries and the Benelux countries. Why have we not started there? Leave that we have not started in US and UK if that have been such a blocking factor that we were operating secondary processing plant there."*¹⁷⁸

The same manager claimed further:

*"At least when we have studied this [that is whether producers could go into breeding] we could not recommend that they invested in this. What has happened now is that one strong producer has from a certain presupposition that he gets from the markets, from the sale office in Germany in this case started to bread fish. This is a strong market for breaded Ocean Perch fillet, and this opens for other options but this has not opened the opportunity for high quantity... The equipment is there and now we can develop the connection with our customers. It is a bit difficult for us as a dealer to take the initiative in this having no fund to put in this"*¹⁷⁹.

In this quotation the manager is referring to Útgerðafélag Akureyringa, which is one of the biggest producers inside IFPC, as it had started to produce breaded fillets mainly of Ocean Perch for markets in Germany.

¹⁷⁷ Interview with former board member of PPCs, I-16.

¹⁷⁸ Interview with managers of IFPC, I-2.

¹⁷⁹ Interview with managers of IFPC, I-2.

The main issue is information, and that through the history of IFPC it has never been considered as an option to go into breeding in Iceland. The above quotation from a manager of IFPC reflects very well one of the main issues in this network, that is, those who had the access to the markets prepared the information for the producers and in many cases evaluated them as well. This is also reflected in a quotation from a manager in one of the PPCs:

“It is not good to have some men in Reykjavík that neither work on the markets or in the production to “pre-cook” the information for producers and the market. There is a danger that you start to doubt how they value the information and what lies behind them.”¹⁸⁰

Due to the conflict of interest between the producers and the secondary processing by the central firm, it is clear that they are in many ways in competition with each other about value creation, which affects the information flow and emphasis on the markets¹⁸¹. IFPC has in some ways admitted this when it split up the UK operation into Coldwater UK, that takes care of the secondary processing, and IFPC UK, that takes care of the resale of products from producers. As one manager of IFPC claimed:

“We have always made the requirement that the secondary processing plants are at arms length.... On the other hand it is clear that we had problems in UK because of great conflict of interest between the part that were operating the secondary processing and the parts who were in the resale. We split this for three months, that is July – August (1998). These two are separate companies in the same ownership that is 75% in ownership of IFPC and 25% in ownership of our Danish partners. These companies have then co-operative guidelines between them, giving Coldwater UK first preference on all what we produce here in the same way Coldwater has to give us first preference on products that they want to buy.”¹⁸²

The same conflict is active between Coldwater US and producers in Iceland although that conflict has not been as much on the table as the conflict in the UK. An explanation of this can be the historically strong position of

¹⁸⁰ Interview with a manager of PPCs, I-8.

¹⁸¹ It is also interesting to point out that a the manager of ÚA during this time had previously been working in the marketing section for Icelandic Seafood a competitor to IFPC.

¹⁸² Interview with a manger of IFPC, I-3.

*"It is not sensible to maintain with hand-power some processing here home when it creates more profit by doing it abroad. On the other hand we can not forget that here at home great opportunities have opened for further processing after the producers have become bigger and stronger."*¹⁸⁵

This increasingly put pressure on the network to create the type of relationship where producers have the opportunity to get access to information and knowledge in the network that can support further value creation in their own companies. This in accordance with the new emphasis in the literature about networks and cooperation, where the value creation is the central issue¹⁸⁶. This puts the emphasis, in analysing network like IFPC, on the "value creation" in the network and the possibility for participants to increase their value creation. Hence, the central issue becomes one of how the participants' companies work together to co-produce value, rather than of how any one company can locate itself in the right position in the network, or of the bargaining power of each actor in the network¹⁸⁷. In many cases the IFPC network has built on being in the right position in the value chain, in the spirit of Porters model¹⁸⁸. According to the interlocutors the conflict of interest has meant that producers are not gaining sufficient access to information and knowledge that is essential for further development and value creation. This can lead to a lack of trust in the participants in the network.

VI.2.2.2 Role of the central firm in the alliance

In interviews, managers of IFPC and its subsidiaries usually defined the role of IFPC as a service company for producers. This can be summarized by a quotation from one manager of IFPC who claimed that the role of IFPC is to:

¹⁸⁵ Interview with Friðrik Pálsson, former president of IFPC and presently Chairman of board of UIFP in Morgunblaðið 13/4 '99.

¹⁸⁶ See for example, Axelsson, B.; Hakansson, H. & Johanson, J., 1988; Larson, S.; Jarillo, C. J.; Easton, G.; Ouchu, W. G.; Osborn, N. R. & Hagedoorn, J.; Clegg, R. S.

¹⁸⁷ Normann, R. & Ramírez, R.

¹⁸⁸ See for example Porter, E. M.

Coldwater US, independence from IFPC and the long-term duopoly of IFPC and IS/SÍS of selling to US.

The case taken here about conflict in the network about breeding in Iceland versus breeding in secondary processing plants abroad is not the central issue in the network. As one manager of IFPC subsidiaries said when he was asked about whether he believed that operation of secondary-processing plants had delayed this development:

*"This case about breeding in Iceland versus breeding in secondary processing plants abroad is not the central issue but the value creation in general. It seems to be obvious that when one of the producers inside IFPC started to bread fish, it opened up these conflicts and it is after that that IFPC recognized these conflicts and split up the reselling and secondary processing in UK."*¹⁸³

When this manager was asked about whether he believed that operation of secondary processing plants had delayed further development in value creation in Iceland he said.

*"Yes I think that this has delayed this development but I am not saying that the secondary processing plant was bad and I am not saying that all producers should be breeding fish. The markets for breaded fish are declining in quantity as well as price rather than on the way up... .. The secondary plants are not only producing breaded fish but also cutting down into smaller portion unbreaded fish and packing. Producers could easily do this in Iceland. The difference between IFPC and Icelandic Seafood is that Icelandic Seafood is not operating secondary processing plants in UK..... Producers inside Icelandic Seafood are producing retail products in Iceland, which they claim are returning them high value... If we look at the value creation (for producers) inside IFPC it is highest on products that are going through the marketing subsidiaries as in Germany, France and even Japan." [Where IFPC is not operating secondary processing plants]*¹⁸⁴

This again put the emphasis on value creation in the network and the environment that the participants' companies are offered. In studying the value creation in this network it is dangerous to be blind and just look at the value creation in Iceland, as Friðrik Pálsson claimed in an interview soon after he quit as president of IFPC.

¹⁸³ Interview with a manager of IFPC subsidiary, I-17.

¹⁸⁴ Interview with a manager of IFPC subsidiary, I-17.

“...guarantee that the producers get the best deal and opportunities on the market in long run¹⁸⁹.”

This raises the question of what is the best deal and opportunity? Asking the managers of IFPC and producers, the first response was usually just *“competitive price”*. Then as the interview went on they started to add that it was not just the price, it also includes guarantee of payment, stocking time, minimum of after sale claim etc. Clearly the price is the single most important factor, but after analysing these interviews, managers of IFPC and producers seem to be unanimous that the best deal includes;

“...competitive price in long term, guarantee of payment, short stocking time of products, short time until the product are paid, quality and minimum after sale claims¹⁹⁰”.

In addition to this, interlocutors talked about the role of IFPC being to offer the *“best opportunity”* on the markets for producers. This included that IFPC had to offer producers new opportunities for their products, as well as opportunities to increase the value of their productions. In order to make use of the *“best opportunity”* and *“best deal”* on the market the quality and response time of information that IFPC is returning to producers is vital¹⁹¹. This makes great demands on the effectiveness of communication and IT system used in the relationship. The best opportunity is also closely connected to the previously described value creation in the network and the conflict between IFPC and producers there. It is therefore clear that these conflicts between actors that influence the information flow and the value creation in the network can affect the ability of IFPC to fulfil its role according to the above description (that is, to offer producers *“the best deal and opportunity in long term”*). This role should in many ways rather be counted as an aim or objective of IFPC.

On the other hand is the role of IFPC as a central firm in this network that has changed considerable through its operation time. The role of IFPC is reflected in the form of the alliances and was discussed earlier in this

¹⁸⁹ Interview with a manager of IFPC, I-4.

¹⁹⁰ Based on interviews with managers and staff of IFPC and producers.

¹⁹¹ Based on interviews with managers of IFPC.

chapter. In the first period (that is in 1942 – 1962), the main role of IFPC was twofold: to sell the producers products and to take care of interest matters of its members. As has been previously discussed IFPC suffered from being the “child” in a joint venture that was dominated by its “parents” during this time. Hence, IFPC did not have a clear role in governing the network during this period. The role of IFPC was to coordinate activities such as to implement collective quality and packing systems. The next period is from 1963 – 1986, when IFPC is clearly the ruling actor in the network by controlling sales and taking care of interest matters of its members. After 1986, the new chairman of board and president implemented a new strategy. This is reflected in moving sales to the markets into the marketing subsidiaries, leaving IFPC with no actual sales (that is, no core activities), as was bemoaned by a former manager of IFPC:

“Now they have even taken from me the permission to sell”¹⁹²

In many ways, 1986 is the turning point in the role of IFPC. The development of moving sales completely to the marketing subsidiaries took some time and was not complete until after 1990 when IFPC had established marketing offices in France and Japan. This leaves IFPC more or less with just support activities for the network, having moved the core activities to the markets. Other changes during this time were, for example, that IFPC stopped acting as a pressure group for its members, and also that they cut down their connection to companies in related businesses such as in the packing and transportation sectors.

At the same time as the role of the IFPC in the process from producers to the markets has increasingly moved into supportive activities and coordination, producers have increasingly merged, becoming stronger and better qualified to take on demanding activities. In similar ways the marketing subsidiaries have gained more experience and knowledge of the markets than IFPC itself. The status of IFPC after this is reflected in a quotation by a manager of PPCs:

¹⁹² Interview with a former manager of IFPC, I-4.

*"The sale organisation and especially IFPC are going through middle age crises similar to what humans go through. This reflects in being grown up and the youngster matured leaving the question of how much freedom should we give them. This entails that for IFPC it is difficult to free the hand of producers and its subsidiaries."*¹⁹³

This captures very well the situation that the central firm is in, that is, with no core activities in value creation. Rather, the central firm has supportive activities that many producers view as a cost in the process rather than creating.

It is interesting in the history of IFPC that producers have in many cases applied pressure to make changes in the role of IFPC as the central firm. This was reflected in 1980 when producers put pressure on IFPC to put more emphasis on new markets. This was then taken further by moving sales to the marketing subsidiaries, which was done more or less according to the strategy, which was laid down by the new president of IFPC in 1986. As has been said before, this left IFPC with only supportive activities, and the difficult position of having the subsidiaries with independent boards of producers and the chairman of IFPC as the chairman of the board of some of them¹⁹⁴. Hence, the presidents of IFPC, and IFPC itself, have in many ways limited authority in governing the network. This is one of the central issues in the criticism of IFPC that led to changes of the chairman of the board and the president of IFPC in spring 1999. There again producers applied pressure to make changes in the role of IFPC, especially the Mother company.

The changes in 1999 include for example, that the president of IFPC will be the chairman of the board of each subsidiary, and that the board of each subsidiary will become an executive board instead of a producers' board. This will increase the governance role of the Mother company and the authority over the subsidiaries, but it is difficult to see how it will increase their independence. What is likely to happen though is that the Mother company will no longer interfere with every sale and therefore be an

¹⁹³ Interview with a manager of PPCs, I-8.

¹⁹⁴ Chairman of IFPC board was also chairman of IFPC subsidiaries that operated secondary processing plants.

intermediary between the subsidiaries and producers. In many ways this will not change the role of the Mother Company of IFPC in the network, which is to govern and coordinate the network. This will instead change the methods used to fulfil the role and will be looked at later in this analysis. It is claimed here that the role of IFPC as central firm has mainly been to coordinate activities and govern the network. On the other hand the main aim of IFPC has been to “*offer producers the best deal and opportunity on the markets in long run*”. In the following discussion about the governance of the alliances, deeper analysis will be performed on the methods of governing the alliances and influencing factors on that.

VI.2.2.3 Governance of the alliances

VI.2.2.3.1 Mechanism

Yves L. Doz pointed out that the “*operating interfaces between the two partners cannot be left to chance and to ad hoc adjustment*”¹⁹⁵. Instead, clear internal organisational relationships, as exist in strategic alliances, demand some kind of administrative mechanism¹⁹⁶ to be able to share information and knowledge as well as coordinating activities,¹⁹⁷ with the overall aim to make the strategic alliances efficient and competitive. Hence, in networks with high numbers of participants the administrative mechanism has to be effective and able to cope with different aims and strategies of participants’ companies. One of the managers of IFPC framed this as:

*“It is a fundamental issue that we (the Mother Company) keep eyes on the operation otherwise we cannot evaluate whether we should operate all our subsidiaries abroad. Likewise, it is essential for this company like others to have some kind of central overhead. Complete decentralisation was out of fashion a long time ago; it was a long time since it was abolished”*¹⁹⁸.

¹⁹⁵ Doz, L. Y., page 337.

¹⁹⁶ Axelsson, B.

¹⁹⁷ Johnston, R. & Lawrence, R. P.

¹⁹⁸ Interview with manager of IFPC, I-3.

More or less until 1986 all communication and physical flow of products were controlled through the Mother Company, and direct connection between producers and marketing subsidiaries was not appreciated¹⁹⁹.

One of the main characteristics of the administrative mechanism of IFPC and its subsidiaries is the independence of each subsidiary through a board dominated by producers. This raises the question of why this has developed this way? From interviews with managers of producers' companies it seems clear that this in many ways was done to build up some form of marketing knowledge by producers, as well as to guarantee that they had understanding of what was happening on the markets²⁰⁰. If managers from the Mother Company had dominated the board of each subsidiary and therefore governed them, the producers would probably have viewed that as too much power and authority for the Mother Company in this process. That could have lead to a lack of trust between these two sectors instead of mutual understanding of what was happening each time. This can also be viewed as a method to coordinate and build up an informal shared vision. This can be seen from a quote from an interview with a former manager of PPCs:

*"It is clear that being a member of the board of IFPC and its subsidiaries was for many managers of production companies essential to be in touch with what was happening on the markets. In that way we got direct contact with the people working on the markets, not just the people in Reykjavík."*²⁰¹

This independence of the subsidiaries often meant that the Mother Company lacked formal authority both over its subsidiaries and producers to control the process. Hence, this makes it difficult to locate the mechanism on the two dimensional scale of markets and hierarchy²⁰². It is rather through the scale put forward by Ouchi (1980), which approached this problem by adding a new dimension that builds on cooperation²⁰³ (see picture V.4 in the

¹⁹⁹ Based on interviews with managers and employees of IFPC and PPCs.

²⁰⁰ Based on various interviews.

²⁰¹ Interview with former managers of PPCs, I-12.

²⁰² Axelsson, B.; Hakansson, H. & Johanson, J., 1988; Larson, S.; Jarillo, C. J.; Easton, G.; Osborn, N. R. & Hagedoorn, J.

²⁰³ Jarillo, C. J.

Literature Review chapter). Ouchu approaches this by splitting the hierarchy into two parts, the “bureaucracy” which would reflect the traditional hierarchy and the “clan” which describes long-term relationships, carried out through non-specific contracts within the formal environment of an organisation²⁰⁴. Until 1986, the main characteristics of the administrative mechanism of the IFPC network were centralisation of information and knowledge through the Mother Company. Despite the lack of formal authority and power in the process, the Mother Company was in a central position to govern and coordinate in the process. Hence, it is clear that the Mother Company, through its central position, had much more power and authority than the theoretical picture indicates. Due to all this the administrative mechanism of IFPC can be located in the clan group on this scale, where they use the methods of a vertically integrated firm through coordination instead of formal authority, as vertically integrated firm would have done. In many ways these methods are understandable considering rather small number of markets that IFPC were operating on and that the Mother Company itself took care of a big part of the sale, that is, its core activities.

After 1986 these methods and mechanism started to change, mainly due to the moving of core activities to the markets, leaving the Mother Company with supportive (and governance) activities. In many ways an internal market emerged by the increased numbers of marketing subsidiaries that were competing with each other for products from producers; this can be seen from quotations from two managers of IFPC subsidiaries:

“...we are in constant competition with other markets areas...”²⁰⁵.

“The competition between subsidiaries blocks, in many cases, cooperation between them”²⁰⁶.

Due to that, the emphasis in the administrative mechanism moves from just coordinating activities between it and producers to coordinating activities of

²⁰⁴ Jarillo, C. J.

²⁰⁵ Interview with a manager of IFPC subsidiary, I-1.

²⁰⁶ Interview with a manager of IFPC subsidiary, I-15.

the subsidiaries to the producers. The Mother Company did this through the authority of having to agree on each sale. In an interview with a manager of IFPC he stated that:

*"The issue is this [the need to get agreement from the marketing division for each sale] is not just to be a barrier in the system as a whole telling you whether you can or can not, rather it is the marketing manager of IFPC that is responsible for the sale contract to be fulfilled or not. Therefore the sales person can be relaxed and say to his customers that it is okay with the order.....and then it is the marketing manager of IFPC that evaluates the contract and says yes it is okay then he is responsible for fulfilling the contract and guaranteeing that producers will produce the product"*²⁰⁷.

Another manager in the Mother Company framed this part of the control in the following way:

*"We here [in Reykjavík] are thinking about the producer- his needs, his wishes, and his opportunity on the markets. We build on this when we go to the sale person to keep them concentrated to the main issue. The sale person on the other hand should think about the customers, the opportunities and danger on the markets and the daily sale operation"*²⁰⁸.

From this quotation, it seems obvious that inside the Mother Company managers view this control over sales as a method to avoid internal competition as well as to coordinate activities between the marketing subsidiaries and producers. This can be seen in a quotation from a manager of an IFPC subsidiary:

*"There is no one in Reykjavík deciding on how or what we do here. Contracts go home to start certain processes. No contract goes home without us being sure that it will not be stopped. On the other hand when it goes home then they push the buttons to start processes such as documentation and transporting. In addition, even before we sign the contracts they connect producers to the contract"*²⁰⁹.

It is clear from interviews with managers in the producing sector that they on the other hand criticised this mechanism as being too centralised and blocking direct communication between the producers and markets²¹⁰. They experienced that in many ways they were pushed to use the central body to

²⁰⁷ Interview with a manager of IFPC, I-2.

²⁰⁸ Interview with a manager of IFPC, I-4.

²⁰⁹ Interview with a manager of IFPC subsidiary, I-17.

²¹⁰ Based on interviews with managers of PPCs.

get information, as the following quotation of one manager of PPCs demonstrates:

“IFPC has built up too big a body in Reykjavik, that is, the marketing division and R&D division, that in many ways are an unproductive operation between the markets and producers. It is essential to have direct communication between producers and the markets. It is not good to have some people working in Reykjavik who are neither working in the markets or production- pre-cooking the information for producers from the markets. There is a danger that producers will doubt their judgement of value behind their decisions”²¹¹.

This reflects the fact that the Mother Company coordinates all activities through centralisation of the information flow from the markets to producers and vice versa.

In a similar way another manager of PPCs stated:

“By agreeing on all sales, IFPC MC is taking on responsibility for producers and subsidiaries that often is difficult to fulfil. It is vital for us producers to be responsible for our marketing operation due to increased competition and pressure from our shareholders for good results. Therefore both producers and the subsidiaries need to be responsible for their own operation.”²¹²

On the other hand, managers of IFPC point out that they have examples where salesman had got a producer to agree on the sale of a product that the market division stopped, and pointed out that they (the producers) could get a higher price for the same product on other markets²¹³. This causes dissatisfaction for the sales person, but points out clearly the internal competition within the network. In the same way, this raises questions of the importance of coordinating information when more and more of the sales are through direct purchase of the subsidiaries for resale, making the transparency of the sale unclear. If the Mother Company did not have this coordinating role between the subsidiaries and sales, it would increase the danger that the subsidiaries would try to purchase the products cheaper and sell them for higher price. As one former manager of PPC stated:

²¹¹ Interview with a manager of PPCs, I-8.

²¹² Interview with a manager of PPCs, I-20.

²¹³ Based on interviews with managers of IFPC, I-2 and I-3.

*"It was well known that we suspected that the price of the products increased at sea in the transportation. If the subsidiaries purchase the products completely they will definitely try this more and more"*²¹⁴.

In many ways, the administrative mechanism of IFPC has not changed much from 1986. It is still based around the Mother company although the emphasis has changed in accordance to changes of the operation. The main characteristics, of the mechanism, though, are more or less the same, based on the centralisation of information. The changes of the ownership form of IFPC have not changed this much, rather it changed the relationship with the producers in that sense that producers were not as dependent on IFPC as before. The changes of dependency in many ways can affect the mechanism by making producers more opportunistic in the relationship, which puts pressure on the mechanism to meet producers' needs faster. Other factors that affect this mechanism and have created pressure on IFPC included the fact that producers are becoming bigger and financially fitter, and that general knowledge inside their companies has greatly increased. This can be seen from a quotation from one of IFPC's managers.

*"What we still find is the criticism that we are looking at these days is that with increased education in the production companies and younger people they find that they should utilize these people to have more knowledge about the markets and therefore the marketing division will be in their way. It is neither good nor exciting enough to talk to people in Reykjavík instead of talking directly to the sales man out on the markets. This happens although it is known that the marketing division has a much better overview. This is called talking to the "sale man" or talking to "the markets". Our strategy is that if they want to talk to the markets they can do that. We do not build some barriers and are more than willing to reduce the staff in the routine job here at home"*²¹⁵.

It is obvious from the previous discussion and quotations that the main criticism of the network concerns the question whether there is centralisation or not. This is also reflected in questions such as how much of the activities should the participants' company take care of, how much should the central firm do and how should the central companies fulfil their roles in the network. One of IFPC's managers stated that:

²¹⁴ Interview with former managers of PPCs, I-12.

²¹⁵ Interview with a manager of IFPC, I-3.

*"It weakens our position if we do not have an overview of all the processes. Then we would be abolishing a knowledge network that has been established for producers and is at least beneficial for the companies that are smaller than the five biggest that is around 20 companies. These companies are considerably smaller and technically worse equipped, although managerially good companies. Their production is not that much so they are very dependent on IFPC. Do the bigger companies want to abolish the smaller firm and let them form a coalition that will be their competitor? Due to the fact that they (the five biggest) are getting that big it is a question what will their ego be, not just in companies needs but also their personal ego. They want increasingly to be in contact with the customers and take part in development project with them.there are producers today that say we have no need for Reykjavík. The subsidiaries are capable enough and we can work with them individually and we can then just choose or deny"*²¹⁶.

The same manager also stated that due to the internal competition there is a danger that this competition would bring the producers a lower price due to a lack of overview of all markets, or as he stated:

"People are human and each sales person is fighting for his area and his customers".²¹⁷

It is clear that there is controversy about this mechanism. In 1999, this controversy is reflected in a planned change, which includes cutting down staff in the marketing division of the Mother Company and increasing the direct connection between each subsidiary and producer²¹⁸. Another interesting aspect of this change is an increased power from the Mother Company over each subsidiary, because the president will be the chairman of the board and each board will only have three members. Hence, the boards dominated by producers are over. This will give the Mother Company an opportunity to coordinate activities through methods other than being "a tube" in the process. This raises questions such as whether the methods of coordinating will change from coordinating through centralisation to coordinating through strategy.

From 1986 until 1999, when the proposed changes become active, the mechanism of the IFPC network is closer to a hierarchy than a free market

²¹⁶ Interview with a manager of IFPC, I-2.

²¹⁷ Interview with a manager of IFPC, I-2.

²¹⁸ Based on interviews with staff of IFPC and Frjáls Verslun.

due to the centralisation of governance and coordination. On the other hand, it is difficult to talk about hierarchy when IFPC lacks the formal authority in the process to control both the information flow as well as the subsidiary sale. There is a paradox in the strong position and the control of the Mother Company of each sale of the marketing subsidiaries and the independence that the marketing subsidiaries have from the Mother Company. In many senses the interface or touching points of actors in this network are twofold, first between the Mother Company and producers and then secondly from the Mother Company to its subsidiaries. A third interface has emerged increasingly from 1986 between the subsidiaries and producers. This interface is on an ad hoc basis and outside the normal structure of how things should have been done.

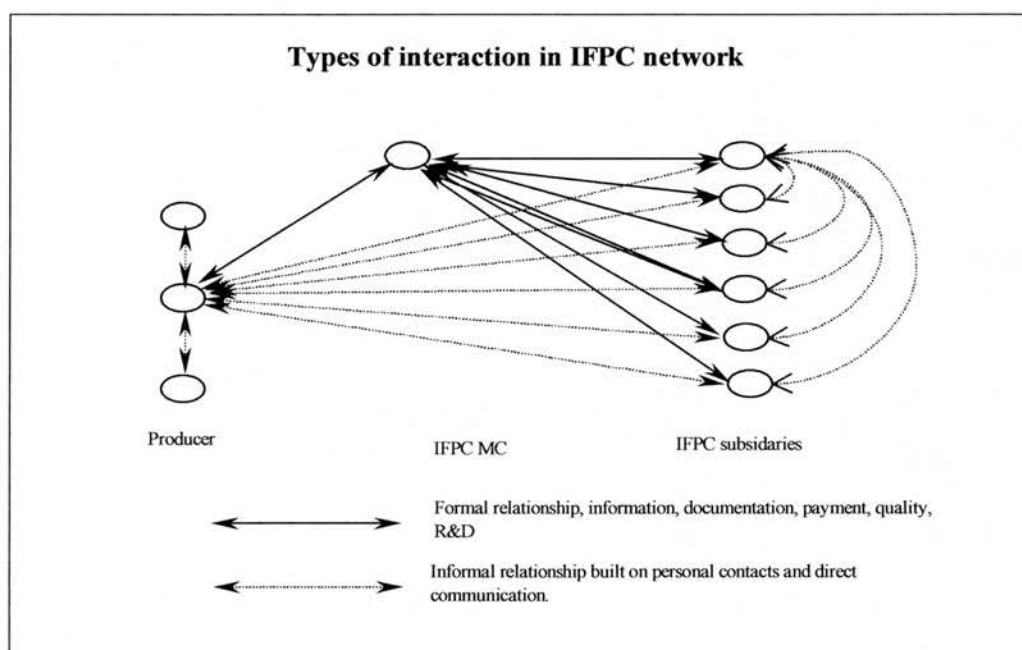


Figure VI.10 Types of interaction in IFPC network

This mixture of mechanisms has in many ways characterised the governance during this time. In reality there are at least two active mechanisms. First is the formal mechanism with the Mother Company in the centre, characterised by centralisation of information and knowledge. Secondly, there is the informal mechanism, that is, direct connection between subsidiaries and producers. This mechanism is characterised by informal connection and personal contacts between managers and staff in participants' companies. One manager pointed out that the form of

mechanism used was connected to the type of product they were selling, or as he stated:

“When we are selling brand products and it does not matter who is the producer, it is produced under the Icelandic brand. Then there is no special need for us to have direct contact to producers when it does not matter who is the producer. Then it is simple for us to talk to one instead of five producers about the same thing”²¹⁹.

On the other hand when the subsidiaries are working with producers on special products or for special customers they claimed that direct contacts were vital for them²²⁰. According to this mixture of mechanisms it is important to keep the mechanism effective. This is also confirmed in a statement from a manager of a production company when he states:

“For the standard products I am happy to get rid of it from my freezer’s doors but for the more value added products and special packing I almost want to know how the consumers chew the products. Therefore I need to have an overview of the whole process and direct communication to the participants.”²²¹

It is clear from interviews with managers and staff of participants’ companies that there are many issues affecting the role of the central firm in the governance of the network. In the following chapter of this analysis, issues that emerge from the analysis of interviews and history will be discussed to give a better picture of the development of governance in the network. The main issues that emerged from the analysis are power, communication and IT, coordination, independence and social maturity.

VI.2.2.3.2 Power

One of the first questions to be asked about a network such as IFPC concerns the power balance and authority between actors in the network. One of the competitors of IFPC’s network claimed that when they introduced them to their potential customers they put great emphasis on being a vertically integrated firm²²². By this they claimed that they have

²¹⁹ Interview with managers of IFPC subsidiaries, I-17.

²²⁰ Based on interviews with managers and staff of IFPC subsidiaries.

²²¹ Interview with producers manager, I-19.

²²² Interview with a manager of competing company to IFPC, I-22.

control over the whole process, which IFPC and IS, their main competitors, have not.

When managers of IFPC and its subsidiaries were asked about whether they lacked formal authority in this process the answers were not unanimous, although they tended to be rather careful about this topic:

“It is a weakness in our system that we were only advisors about what to produce what the price was and what the return price was. It is right to point out that around 1980 we had a productivity department that calculated the productivity of each production method for producers that themselves often used poorly coordinated and primitive technique. I found that many producers used the calculation of the productivity department as the only calculation behind their product decisions.”²²³

This system was more or less active until after 1986 when a new president took over in IFPC, and it was finally abolished around 1990 when the productivity department was abolished and producers were themselves made responsible for their own calculations concerning the production decisions. It is clear during this time that, through the centralisation of information and knowledge, the Mother Company wielded great power even though it was informal. This can be seen from a quotation from a manager of the Mother Company:

“It was this strong centralisation that characterised the company and was even its strength. Producers of “block”²²⁴ did never know how much of the products went to US or Europe; they were paid according to payoff periods and on equalization price. As a salesman I regret this period (the period before 1986) because you could sell on a high price and then on a lower price to customers that you had believed in for a long term and you did not have to talk to producers about this. However, in this time the producers started to demand to produce what was best at each time and to know more about the production and the markets than was published in the monthly newsletter. This was recognised by the new president and changed.”²²⁵

This lack of formal authority affected the long-term strategy in the process. This is because it is difficult to build up markets or products when producers were opportunistic and jumped to better opportunities when they arose, as a

²²³ Interview with a manager of IFPC, I-2.

²²⁴ Block is standard products mainly used for secondary processing.

²²⁵ Interview with a manager of IFPC, I-2.

manager of IFPC stated when he was asked about the producers' commitment:

*"When we talked to the producer today he was very positive but after two weeks his preconditions changed. He saw that it was possible to produce some other products, for example to the US because the dollar became stronger, then the producers told us to find somebody else. Therefore, this weakness always exists."*²²⁶

On the other hand interlocutors pointed out that by connecting producers to the contract they have built up formal authority because the producers need to fulfil the contract. This was confirmed by one of the managers of IFPC when he was asked whether the Mother Company had authority of what producers would produce:

*"Not directly. We cannot promise things without producers' agreement to produce. However, after we have made contracts out in the markets then increasingly we connect the contracts to producers because they sign it and take on all commitments of the contracts. This means that our authority starts there. If the producer does not fulfil the contract the customers can make claims against the producers. In this way the producer has a commitment to keep the contract."*²²⁷

This has brought IFPC an opportunity to gain more authority through contracts. According to interviews with managers of IFPC they claim that producers increasingly ask to receive information and to confirm sales contracts themselves to be better informed about the markets²²⁸. This is also to have more stable contracts to build on and is in accordance with the increased emphasis on special products by producers. It is clear, though, that most of producers' production is unbound to contracts; producers claim that they have less than 10% of their products bound in contracts²²⁹. Hence, producers have all the opportunities they want to swap between markets according to market conditions.

It is clear from interviews with both producers and IFPC staff that there exist both formal and informal mechanisms of authority. The formal one is

²²⁶ Interview with a manager of IFPC, I-2.

²²⁷ Interview with a manager of IFPC, I-4.

²²⁸ Based on interviews with managers of IFPC.

²²⁹ Based on interviews with producers.

based on the rules and constitutions of IFPC that give the Mother Company limited authority in this process. On the other hand there is the informal mechanism that is built on traditional control over information and knowledge and the connection to customers. This is well reflected in a quotation from one manager of the Mother Company, where he states the following:

"Then it is the informal power, which is of course not much. The manager of PPCs can do what he wants to do. Naturally it happens for some reasons that we cannot offer producers a price that is the best or acceptable. Then the producer says 'okay I will produce this' and often this product or party is connected to some other contract. Hence, as in any cooperation the question arises how can we make a combination that will attract so the producers to produce this production for this contract. Then there is some authority involved in that we can offer some opportunities if I put it clear if you produce this we can get another good deal for you. This is not formal authority-this is first and foremost authority that is in the day-to-day operation that people do not talk much about."²³⁰

According to this, the Mother Company has informal authority through the connection to the markets and its role as coordinator of the sales. This can also be seen from a statement from a manager of IFPC when he explained that IFPC as a whole often needed to built up markets by selling on low margins for some time and to gain it back later with a higher price.

"It is our responsibility [to built up markets] of IFPC as a whole, it is done in the markets because they know the customers. There is our power to maintain markets although producers do not understand it for the moment. We have many examples of this."²³¹

Due to a lack of authority, it is clear that the Mother Company has to exercise much more cooperation to be able to coordinate the activities of sales and information flow.

One of the characteristics of the IFPC network was the equality of members, that is, one member one vote. This changed in 1988, moving more formal power to the bigger companies, although with the veto system. After the ownership changed this changed again, or as one manager of IFPC claimed:

²³⁰ Interview with a manager in IFPC Mother Company, I-4.

²³¹ Interview with a manager in IFPC Mother Company, I-4.

“People do not need to be philosophical about power; in limited liability companies there exists no equality. The only equality is how many shares do you own. Your power is in accordance with that. If someone has enough interest and money then he buys a majority share in this company and of course can do what he wants with it. Producers must have made up their mind about this when they changed the ownership form. Now this company is an open public liability company, which means that who offers the highest price gets the share that is for sale.”²³²

Four months after this interview, this happened in the annual meeting of IFPC for the year 1998 when the biggest owner bought an additional 4% share, which was enough for him to be elected as chairman of the board. This was followed up by the expulsion of the president of IFPC. This will lead to changes of IFPC's operation that will bring the Mother Company more formal authority over its subsidiaries and increase the direct connection between producers and the subsidiaries. On the other hand, this will not increase the authority of the Mother Company towards the producers. The increased emphasis on connecting the sale contracts that IFPC is making with its producers brings IFPC as a whole more formal authority, especially if the contracts are bound with certain producers and customers. This indicates that the central firm is gaining more formal authority in the process than they had before. There is a question of how this will affect the network when one or a few actors can dominate the operation of the network.

One aspect of the power balance between actors in this network lies in the right to ITQs, that is the individual transferable quotas. Interlocutors in the IFPC focused on the ownership of quotas and claimed that the real power lay in quota ownership and in the fact that the quota is bound to the fishing vessels. That gives the owner of the fishing vessels a very crucial role when attempting to gain access to the raw material. An example of this can be taken from the previously described race (see chapter VI.2) between the sales organizations, IFPC and IS to keep producers (mainly ÚA) in their business²³³. On the other hand, producers focused on the power that lies in

²³² Interview with a manager in IFPC Mother Company, I-5.

²³³ Based on interviews with managers and staff of IFPC.

the marketing connection and the control of the information flow back to them²³⁴.

To conclude this discussion about the power in the network it is appropriate to quote a manager of IFPC when he talked about the power balance in the network:

*"I am not sure that it is desirable to gain more authority in the process. What IFPC should put emphasis on is the information flow to its producers. Everybody here indoor admit that most of us are equally logical in thinking. It should not matter whether you have all the information here as a marketing manager or in some other role inside IFPC or production managers in some freezing plant to take decisions. On the other hand what has to bind people at the same time as contract is due to the increased competition in the business today, when we have to connect the contract to producers. It is a fact that we need to make the producers responsible for mistakes if they do not produce the products. Hence, on products that are not bulk products like block we need to have producers in the contract."*²³⁵

The manager is pointing out that the producers are mature enough to take their own decisions based on information from the markets. There is therefore no longer the need for the Mother Company to think for the producers and interpret the message from the markets for the producers. This had been done by the Mother Company through the centralisation, which they are now abolishing. This raises questions about other forms of power than lie in the authority and in the coordination role of the central firm. This could be power in the form of being a strategic leader for the network and the role of strategy or vision in the governance of the network.

VI.2.2.3.3 Strategy

The literature in strategic alliances and networking increasingly points out the need for strategic leadership in the network and alliances²³⁶. In the history of the IFPC network, it is in many ways difficult to point out one leader. At first glance, the Mother Company is the most obvious candidate for this role. One interlocutor phrased the position of IFPC in this way:

²³⁴ Based on interviews with managers and staff of production companies.

²³⁵ Interview with a manager of IFPC Mother Company, I-2.

²³⁶ See for example Lorenzoni, G. & Baden-Fuller, C.

"I often compare IFPC to a horse coach in the cowboy's movies where six horses are pulling the carriage and all the horses shared the same reins. In the case of IFPC we do not have the reins but we have lots of horses [that is the subsidiaries] but they all pull in different direction [their own direction] because the reins are missing."²³⁷

The interlocutor is pointing out that the strategy and leadership are missing from the corporate IFPC. Hence, if IFPC as a corporation is missing the strategy and leadership, the same can be said about the network as a whole. This is not surprising due to the previously described lack of authority and power of the Mother Company. In a similar way, a manager of IFPC stated:

"It is difficult to see how we could be leading and have some political influence because we are just a service unit in the ownership of the companies that we should have political influence on."²³⁸

In this statement, the manager of IFPC seems to doubt that the Mother Company has the opportunity to become a strategic leader in the network. According to the interlocutor this is due to the governance mechanism and lack of formal authority of the Mother Company in the network. In many ways this is right, and the structural form of IFPC and the mechanism of authority did not indicate that IFPC had the role of leading the strategy of the network as a whole. This changed partly with the ownership changes of IFPC in 1997, in that the role of IFPC in relation to its producers became clearer and built more upon business principals. The planned change in 1999 will then make the authority of the Mother Company over its subsidiaries clearer and bring the Mother Company formal authority. Hence, if these changes are successful then the Mother Company has gained the formal authority to become the strategic leaders in the network.

Looking back at the history of IFPC and the network as a whole, it can be seen that long-term thinking has been lacking. In the same way leadership has been lacking in the network and therefore no actors have had the role of leading the strategy and vision in the network. This can be seen, for example, from the change in 1980 when producers pushed for more emphasis on new markets, in 1997 concerning the ownership changes, in

²³⁷ Interview with a employee of IFPC Mother Company, I-21.

²³⁸ Interview with manager of IFPC, I-3.

1998 when Coldwater UK was split up into two companies, and changes in 1999 when a number of producers “overtook” the company to implement a new strategy. In all these examples IFPC was reactive, not leading the way for the network.

Almost all interlocutors claimed that there was neither clear strategy nor vision in the network. Interlocutors from IFPC claim that this can be traced to producers who are characterised by short-term opportunists²³⁹. This has to be looked at in the perspective of the economic condition that surrounded the industry, which was not favourable until 1993 due to the lack of economic freedom and high inflation²⁴⁰. Another consideration is the quota system; the declining quotas made long-term thinking in many ways difficult. It is not until the last five years (from 1994-5) that the majority of producers have gained the financial capability and stability to be able to make some serious long term planning and strategic decisions²⁴¹. It is then a question of whether the clear splitting of production and marketing have not influenced this and made long-term thinking and vision difficult. A manager of IFPC claimed that this could be the case, or, as he stated:

*“Of course, this can be the danger but I think it is exactly the same thinking as a big and powerful competitor to us has. I have not heard anything else but he behaves exactly as we do although he is completely vertically integrated from the basics. This is also due to the flexibility in catching and so on.”*²⁴²

According to the managers of IFPC, it is clear that the opportunism of producers has been a barrier towards the implementation of long-term thinking. An example was taken from the new emphasis IFPC France was using in marketing products:

“We gained there strategic thinking and brought it back home to producers but it has to be admitted that we needed to transfer this strategy from one producer to another almost each month depending on when the producer

²³⁹ Based on interviews with managers of IFPC.

²⁴⁰ See the chapter about the Icelandic economy.

²⁴¹ See the chapter about the Icelandic economy. This can also be traced to opening of stock markets and increased freedom of money transfer between countries that has opened new ways for companies to increase their capital.

²⁴² Interview with a manager of IFPC, I-3.

*found new more exciting opportunities through some other marketing subsidiaries.*²⁴³”

Here the manager points out the fact that the producer is not responsible for the marketing operation and the internal market that gives them the opportunity to jump on new exciting opportunities, causing barriers towards strategic thinking. The manager carried on by commenting on the nature of the business:

“What I have been trying to say is that this business is such that we control very little of it. There are some areas that we can control but the business is incredibly opportunistic and some people see it as some kind of “Wild Producers” in double meaning of that.”

Here the manager is referring to catching from wild stocks, and also that the producers are wild in their business. It is also clear that the limited authority is, in his view, affecting the ability of the Mother Company to be a strategic leader of the network.

According to the interlocutors there are many issues affecting the long-term strategy or vision of the network. These issues can be split into two main themes, one relating to the nature of the business and the other to the nature of the network. The nature of the business produces the uncertainty mainly due to fishing from wild stock that affects producers and causes them difficulties in planning. For the bigger producers that are vertically integrated into the fishing sector, uncertainty in this is rather low. They know their quotas, and, although they cannot guarantee, it they fish the right spices at the right time. This means that control and planning of the fishing is getting more accurate and easier. The other part of this is the nature or structure of the network. This is mainly the lack of authority of the central firm that clearly has not had the role in the network to form or lead the strategy of the network. Before the ownership changes the strategy was to serve every member on a more or less equal basis, or as one interlocutor said:

*“The strategy of IFPC has been to be friends of everyone”*²⁴⁴.

²⁴³ Interview with a manager of IFPC, I-3.

This strategy is reflected in the aim and role of IFPC, to be a service company for its members. After the ownership changes this has changed slowly. This has led to a lack of strategy in the network because no one in the network considered it their role to lead it strategically. This can also be traced to the fact that producers controlled IFPC through the board and the board of its subsidiaries.

After the ownership changes IFPC has a business contract with producers, making the relationship a business relationship instead of the mixture of business and social relationships as it was before. Together with the planned change, this brings the Mother Company more opportunity to lead the network with a long-term vision and implement it through its subsidiaries and in their contract with producers. Lorenzoni and Baden-Fuller focus on the importance of creating an atmosphere where the participants' companies can be creative and the network flexible²⁴⁵. The planned change to IFPC in 1999 brings it an opportunity to take more proactive action for the network and lead the strategy to be able to create an atmosphere of flexibility and creativity, instead of trying to control the network through centralisation.

The lack of strategy, and of actors in the network who are responsible for leading the network, has in many ways influenced the IFPC network. The impacts have been obvious: IFPC has been conservative and re-active to respond to changes. In many cases this can be traced to the structure of the network where the formal authority belongs to producers and the governance mechanism is based on centralisation. Whether clear strategy and leadership from the central firm could reduce the need for centralisation and increase the flexibility in the network is difficult to judge from the IFPC cases, but the need for it is obvious.

VI.2.2.3.4 Knowledge, Communication and IT

According to interlocutors, effective communication is essential for networks such as IFPC. From the analyses it is clear that the network has

²⁴⁴ Interview with a former member of IFPC board, I-16.

²⁴⁵ Lorenzoni, G. & Baden-Fuller, C.

changed much more into a business relationship instead of the social relationships that previously existed. These changes have simultaneously brought changes to the communication in the network. Before 1986 most of the communication went through the central firm, or as one interlocutor stated:

“If we come back to the old managers, many of them were in the board and were updated on the monthly board meetings about the status of the markets. Others were quite happy to telephone here and get information of what they should produce and the time until the products were shipped. Then they found it sufficient to talk to 2-3 people here in Reykjavík that had an overview over what was happening.”²⁴⁶

With changing generations in the production sector and in IFPC this has changed. In a similar way, another manager of IFPC stated:

“What has happened is that before producers had little market knowledge but now the world is much smaller and we have our information system open. This is what members wanted when they existed and this is what the owners that is, the producers want now. By doing this the producers can build up their knowledge of what is happening on the markets. This is happening now, not much but more than we have known before. They watch more and more what we are doing. It is therefore open communication: when we talk about price they know what price we are referring to.”²⁴⁷

It is interesting to see how managers of the central firm talk about direct communication but at the same time were operating communication systems that were built around centralisation of information through the central firm. On each site of the central firm both producers and managers in the subsidiaries claimed that the central firm was struggling to keep up the centralisation of information flow and communication²⁴⁸. It is a question whether this can in some ways be traced to the lack of a well-defined role for the central firm in the process. On the other hand, Lorange P. and Roos J. point out the need for someone to coordinate activities to avoid information asymmetry²⁴⁹. They point out the use of strategic planning to do that, which is missing from the IFPC network. Hence, it is concluded

²⁴⁶ Interview with a manager of IFPC, I-2.

²⁴⁷ Interview with a manager of IFPC, I-4

²⁴⁸ Based on interviews with managers and staff of IFPC and its subsidiaries and producers.

²⁴⁹ Lorange, P. & Roos, J.

here that the *lack (of a) defined role of the central firm as well as inadequate authority and lack of strategy leads to more centralisation of the governance mechanism in matters as communication and information flow than would otherwise be necessary.*

Although the relationship has moved on to more of a business relationship, interlocutors were unanimous that personal communications were essential to build up trust and the will to work together. This is reflected in the following statement:

“I am not saying that the importance of trust and personal connection have declined. It is more the methods used and preconditions for decisions which are becoming much more economical for their own companies. At the same time there are many more demands from the owners of their companies. They make much higher demands to know more about the markets, the sales, and about the customers than the earlier generation of managers”²⁵⁰.

All interlocutors talked about direct communication and the need to talk to the person who has the information or the authority to make decisions, as can be seen from this statement from a manager of IFPC:

“I define that people want to talk to the person who has the authority to make a decision. Moreover, I have to admit that the man who has the authority to make decisions about production is the product manager and the man who is best informed about what to sell is the sales man. Therefore, we have this development into direct communication. On the other hand, with 20 – 30 producers and large numbers of sales people it is not very sensible to let them talk together all the day. It is not very economical.”²⁵¹

Here the manager points out the need for direct communication, but at the same time points out the danger that this communication can in some cases not be very economical for the network. In a similar way, a manager of one of the marketing subsidiaries claims:

“If we have standard products, no matter who produces them and the products are under the Icelandic Brand name, then there is no special need for us to contact producers on individual bases. It is much simpler for us to contact one instead of five that are producing exactly the same products”²⁵².

²⁵⁰ Interview with a manager of IFPC, I-2.

²⁵¹ Interview with a manager of IFPC, I4.

²⁵² Interview with a manager of IFPC subsidiary, I-17.

In a similar way, a producer pointed out its different needs regarding its different products:

“For the standard products I am happy to get rid of it from my freezer doors, but for the more value added products and special products I almost want to know how the consumers chew the products. Therefore I need to have an overview of the whole process and direct communication to the participants”²⁵³.

From these quotations it can be concluded that a mixture of direct and central communication would fulfil the aims of both producers and IFPC. It is more likely, however, that producers would like to have direct communication with the person that has authority to take decisions about the price and sale. Therefore it could be economical for the IFPC network to have centralisation in the purchase of standard products no matter whether they are sold in, for example, the UK or the US, and then to have direct strategic alliances and communication between producers and marketing subsidiaries concerning more value added special packing.

VI.2.2.3.5 Social maturity and trust

One of the most interesting factors that emerged from this analysis was when interlocutors talked about what could be called fashion and social maturity. From the interviews it was clear that most of the interlocutors, both inside IFPC and producers especially the younger ones, showed great individualism and focussed very strongly on the performance of their companies almost without regard to whether that would affect some other or even their own business in the long run. This was apparent in what could be called “fashion” and framed as *“this is the way we do business today”*. On the marketing side this appeared as the general belief that in order to make profit you have to buy the product for further sales instead of selling it through commission sale. This means that the transparency of the transaction is gone, which could easily damage the trust between participants. On the other hand the freedom and increased competition make this not as serious as it would otherwise be.

²⁵³ Interview with manager of PPCs, I-19.

Managers of IFPC pointed out the danger that will follow the trend where participants stop to think about the interest of the whole and instead think about their own narrow interests, as can be seen from the following statement:

“There is a danger of producers forming a coalition and it is clear that all the producers have not the maturity to think about the interest of the whole instead of their own narrow interest.”²⁵⁴

This raises a question about the nature of a network like this. Is it, for example, likely, that producers will participate in a network if it will not fit to their own aims and strategy? According to producers this is not likely, and it seems to be clear that they are willing to work with the marketing subsidiaries in marketing their product in the long run, but clearly it has to be to their own benefit and has to fulfil their own strategy. Hence, this will increase the need for a flexible network to meet the different needs of participants' companies.

The individualism that the author observed is in accordance with the development in the network. The network is moving towards an open market from the hierarchy where participants' companies have the freedom to choose and where the benefits of participating in the network are evaluated on the basis of competition. It is not unlikely that, due to the newfound freedom, many participants' companies will try to experience the markets on their own to get a feeling for what is happening there. Despite this individualism, social maturity has played a big role in the operation of this network, as can be seen from quotations:

“Although IFPC did not control the production, managers of IFPC understood very well its role and many big producers were loyal when for example, IFPC needed one container then it was possible to talk to few producers and ask them to produce their wanted quantity and this was usually easy.”²⁵⁵

“Naturally it happens for some reasons that we cannot offer producers a price that is the best or acceptable. Then the producer says ‘okay I will

²⁵⁴ Interview with a manager of IFPC, I-3.

²⁵⁵ Interview with a manager of IFPC, I-2.

*produce this' and often this product or party is connected to some other contract".*²⁵⁶

This indicates that producers had the social maturity to make an adjustment to their production to solve problems that occurred in the network. This adjustment between producers and IFPC is based on trust and personal contacts between managers of IFPC and its subsidiaries and managers of producers' companies.

When the interlocutors were asked about whether the increased individualism and economically based decisions had changed the importance of trust and personal connection in the network, the answer was "no". Still they claimed trust that was built on personal connection and experience was also very important in the relationship in the network.

VI.2.3 Conclusion

In concluding this analysis of the IFPC network, one of the first matters that occur is the question of why the network has been so conservative and reactive to changes in the environment. One of the most obvious causes for this is the form of IFPC in the way that it was until the 1999: that is, largely a production-driven network. This is based on the fact that IFPC for most of its operation time has defined its main role to be a "*service unit for producers*". It is not until 1999 that there are changes in the way that IFPC defines its role, which is now as an "*international marketing company for fish*"²⁵⁷. This conservatism can also be traced to a lack of freedom inside the network and to the fact that the network did not have to face real competition from other sales companies. Enforcing producers to sell their product through IFPC has on the other hand, meant that IFPC has been forced to sell all their products. Hence, the network has mainly been driven from the producers' needs rather than the needs of the markets.

The paradox in this is that nobody but producers themselves could change this, and nobody but producers themselves put this enforcement on. This leads to looking at the fact that until 1999 nobody regarded it as their role to

²⁵⁶ Interview with manager in IFPC Mother Company, I-4.

²⁵⁷ Interview with Róbert Guðfinnsson, chairman of the board of IFPC.

lead changes in the network. Until then, no owner had a leading share in IFPC, and even before IFPC became limited liability company equality between producers made this difficult. This has led to a clear lack of leadership in the network, and indicates the need for someone to have a defined role in leading the network. This supports the increased emphasis in the literature about networks and the need for a leading company in the network, as, for example, Lorenzoni G. and Baden-Fuller C., point out with the “strategic centre”, Jarillo C. J. with the “hub” firm²⁵⁸, Easton G. with the “focal” firm²⁵⁹ and Grandori A. with the leadership of a central firm in a constellation for the organisation²⁶⁰.

Academics have increasingly pointed out the importance of informal governance and communication mechanisms in the operation of network. This has been framed as the need for mutual adjustment²⁶¹, personal coordination and communication²⁶², personal networks²⁶³ and processes of mutual adaptation and learning²⁶⁴. The results from the IFPC case support this, as emerged from the analysis that both formal and informal mechanisms exist in the network. The informal is based on personal communication and trust that leads to mutual adjustment of participant companies in the network. By this the IFPC case supports the view that governance in the network is based on both formal and informal mechanism²⁶⁵.

It is interesting to recognise that in the IFPC case the formal mechanism of centralisation worked against the increased tendency to use the informal mechanism. Partly this can be explained by the need of the IFPC MC to withhold power through centralisation and the general belief inside IFPC that the MC needed to coordinate activities through centralisation of

²⁵⁸ Jarillo, C. J.

²⁵⁹ Easton, G.

²⁶⁰ Grandori, A.

²⁶¹ Lorenzoni, G. & Ornati, A.

²⁶² Alter, C. & Hage, J.

²⁶³ Benassi, M.

²⁶⁴ Lundgren, A.

²⁶⁵ See for example Lundgren, A.; Alter, C. & Hage J.

information. In this way, the IFPC case support Pfeffer when he points out that power in a network is often gained from centralised control or coordination over other participants in the network²⁶⁶. Throughout its history IFPC MC has done both these, especially after 1986 when the MC is left with only supportive activities and a lack of defined role in the network.

Lundgren points out that mutual adjustment and learning are the driving forces for changes of the structure of networks, and that a perfectly coordinated and balanced network is a static network²⁶⁷. In contrast, the IFPC network is neither perfectly coordinated nor balanced, but a static network. One explanation of this can be the lack of balance of power and the dependency between actors in the IFPC network mainly in the form of the lack of formal authority of the IFPC Mother Company over its subsidiaries and its lack of a defined role in the network. This has meant that IFPC Mother Company has been a barrier against changes in the network, in harmony with the informal mechanism that has existed in the network. In this way, there has been a change on the network and mutual adjustment, but that has been exercised outside the formal mechanism.

Lorange and Roos point out that companies, and particularly the central or focal companies in strategic alliances, tend to have some “black box” where they protect unique proprietary skills and know-how from other companies in case of a break-up of the alliances²⁶⁸. In the IFPC case this black box can be seen as the brand names and marketing connection that clearly is in the ownership of IFPC. In a similar way Lorenzoni and Baden-Fuller claim “*to maintain the balance of power in the network, all central firms retain certain activities. The control of the brand names and development of the systems that integrate the network are two activities that give the organisation a pivotal role and allow it to exercise power over the system*”²⁶⁹. Due to its lack of formal authority, IFPC has not been in a position to do this, but after the planned changes in 1999 when IFPC MC

²⁶⁶ Pfeffer, J., 1987.

²⁶⁷ Lundgren, A.

²⁶⁸ Lorange, P. & Roos, J.

²⁶⁹ Lorenzoni, G. & Baden-Fuller, C., page 153 –154.

gained more formal authority and role to govern its subsidiaries, they have the entire precondition to develop the system or create the environment that is necessary in this network.

One aspect of this power balance is the power that lies in the hands of the quota holders in the Icelandic fish industry. The previously described race about the business relationship with one of the biggest producers in the fish industry, ÚA, proves that the access to the fish stocks has become a major issue in the network. This access to the fish stocks in the form of quotas could be regarded as the “black box” of the owners of the fishing vessels. The high vertical integration in the Icelandic fish industry maintains certain power between the fisheries sector and the processing sector and helps the producers to retain their power against the exporting companies.

It is clear that until 1999 a power struggle has existed between more or less all actors in the IFPC network. One aspect of this power struggle, and the role of IFPC MC in this process, is the transfer of knowledge inside the network. IFPC MC maintained its status by blocking information and direct contacts between producers and the sales subsidiaries. This was done through the role of IFPC MC as the coordinator and as the point through which information from the market was served to producers. This supports Pfeffer when he claimed that power in networks often arises from centralised control or coordination over other participants in the network²⁷⁰. On the other hand, this has affected the flow of information and learning in the network. Nearly all of the knowledge that IFPC MC returned to the producers was second-hand from the markets in the form of production instructions and newsletters. The centralisation of information has therefore blocked for transfer of the embedded knowledge, which can arise through direct communication between actors in the network. Badaracco described the embedded knowledge as a “*specialised relationship among individuals and groups and in the particular norms, attitudes, information flows, and ways of making decisions that shape their dealings with each other*”²⁷¹. From the analysis it is clear that producers do not want some central firm to

²⁷⁰ Pfeffer, J., 1987.

²⁷¹ Badaracco, J. L. Jr., page 79.

think for them and “pre-cook” information as IFPC MC has done through its history. Producers want to be able to build up their own knowledge about the markets, which they have increasingly done through direct connection with the markets and thereby starting to build up embedded knowledge and feel for the market instead of building solely on information from IFPC MC. One interesting aspect of the knowledge transfer is how little flow of staff there is between the production sector and the markets. This is especially true about the flow from the markets to the production companies. This is slowly changing in that few employees from IFPC and its subsidiaries are now working for the producers. This indicates that market knowledge has not been moved from markets to producers. This also suggests a difference in culture between the production and marketing sectors, built on the clear division of activities between these two sectors and the interference of the central firm.

From the previous discussion it becomes obvious that one of the single most important factors in creating and operating a successful network is to create an environment for participants’ companies to work in. From the IFPC case, it is clear that it is not the formal mechanism of rules and hand-controlled coordination that is the essence of the governance in the network; it is rather the informal network built on trust and direct connection between actors. Lorenzoni and Baden-Fuller support this when they emphasise that the role of the strategic centre is not just to coordinate and rule the network, but rather to create an atmosphere where the participating companies can be creative and where the network can be flexible²⁷². What is not always clear, though, is what is included in the atmosphere and flexible network and what is then included in the role of the central form in creating such an environment. From the IFPC case, three main factors concerning this environment emerged: first is the value creation in the network, second is flexibility and freedom, and third is direct communication and connection.

The first factor is the value creation in the network and the possibility of participants’ companies to increase their value creation. In the IFPC case, the environment has not been favourable for the producers in this matter,

²⁷² Lorenzoni, G. & Baden-Fuller, C.

due to a conflict of interest between IFPC and its secondary processing and producers. From the IFPC case it is also clear that products can be split into two main groups, that is, standard products that could be sold on the trade market and special products (that is, value added products) where producers need to be involved in all steps in the value chain. The conflict between secondary processing by IFPC and producers is obvious and has in many ways delayed further value creation by producers. IFPC has recognised this problem and approached it by separating resale and secondary processing in the UK.

Advocates of free competition claim that this conflict of interest is no problem, and that the freedom to choose and competition will solve this. Hence, if IFPC does not offer the best deal or price then the producers will go somewhere else. This will create pressure on IFPC to offer the best deal. It is claimed here that this would increase the opportunism of producers and change the relationship into an ad-hoc business relationship that is unlikely to increase value creation in the network in the long run. It is more likely that IFPC will focus on how to create the environment where participants' companies can work together to create and increase the value creation in the network as a whole, so all participants' companies will benefit. A precondition of this is the need to deal with the conflict of interest in the network that is affecting this, and to ensure that the network will become market driven instead of production-driven, as it has been. This can be done by increasing the emphasis on the marketing subsidiaries and their connection to producers in marketing their products. From observing the operation in the network, it became clear that interlocutors very seldom talked about marketing of the products, but just about selling products. When this became clear interlocutors were asked about this, and most of them claimed this was due to the lack of stability of the producers caused by their opportunism. Hence, the emphasis was not on marketing fish products but rather just selling the products.

The second factor is the flexibility and freedom in the network. It is perhaps a paradox after talking about the need for stability and value creation to talk about the freedom to leave the network. Interlocutors claimed that it was

important for the network and IFPC to be facing competition where participating companies would evaluate their participation in the network on the basis of competition instead of being enforced to participate. In addition, the freedom will keep IFPC on a constant search for the best way to operate its business, which will drive forces for changes; the endless search for that is the best environment to operate in. In a network like IFPC, with a high number of participants many with different strategic aims and resources, it is important that the network is flexible to be able to fulfil the different strategies of the participants' companies. Hence, lack of resources by smaller participants' companies can mean that they require more service. This has been the case for IFPC but IFPC MC has more or less treated all producers in the same way regardless to their needs. Therefore, in a network with a mixture of small and bigger companies, it is essential to have a flexible mechanism to meet the different needs of individual participants. This differs from strategic alliances or networks with fewer participants that often have a narrower scope and are often bound to certain projects. Such alliances or networks demand a much simpler mechanism of operation than networks with a high number of participants.

The last part in this discussion about the environment concerns direct connection and communication between participants in the network. From the IFPC case, it became clear that both producers and the sales people put great emphasis on the importance of direct communication between actors in the network. The direct communication was the essence of creating trust between actors in the network that leads to will to make mutual adjustment between the companies. On the other hand intermediates in the form of a central firm without some value adding activities as IFPC MC can lead to lack of trust in the values that lie behind the information that is given to producers. The lack of direct communication, and the emphasis on serving and "pre-cooking" information and thinking for the producers, has acted as a barrier towards learning and knowledge creation by producers.

To conclude this discussion about the environment it is claimed here that IFPC and its owners have not put enough emphasis on creating a suitable environment for the actors in the network to work inside. IFPC has put too

much emphasis on offering producers the best deal in terms of price and on serving the producers instead of creating a system where participants' companies can mature and think and act for themselves on their own terms.

Research on networks and strategic alliances has pointed out that such inter-company relationships have moved from formal product-driven alliances towards more informal ones²⁷³. This development seems to be suggesting that alliances are becoming more informal, knowledge-based, objective and market-driven than they were in the past. The development of IFPC is clearly in this direction, that is, to a more informal network. It is difficult to say whether it is becoming more marketing driven instead of production driven network but it is clear that the informal mechanism in the IFPC network has pushed much more towards becoming a marketing-driven network. While as the informal mechanism has been more focused on building up knowledge by direct communication with the markets, meanwhile the formal mechanism is much more information based rather than knowledge-based.

The conclusion from the IFPC case is that it is essential for marketing networks that cover multiple steps in the value chain to have strategic leadership where the main aim is to create an environment that is flexible, within which all the participants' companies can operate and fulfil their own strategy and goals. This network has to be marketing-driven, focusing on the opportunity of the participants' companies to increase their value creation, and on all the steps in the value chain working together to create value instead of destroying value by blocking knowledge from moving freely between actors in the network. A pre-condition to this is the freedom to choose: that is, that the network has to compete with its competitors and other options for the participants' companies. Hence, inside the network the competitiveness is built on cooperation between the actors with the emphasis on creating competitive supply/value chain, but what keeps the network together is the continuous evaluation with other competition. In this way, the network will be in an endless search for better ways to operate its business and avoid the stagnation that has characterised the network of

²⁷³ Shaugnessy, H.; Axelsson, B.

IFPC. To be able to do this it is necessary that there is some owner of the network or some central firm that has a well-defined role to lead the network. It is clear, although the governance is based on an informal mechanism, that without the overall leadership and some formal mechanism it is likely that the governance will be based on putting out fires that arise from a lack of overall aim and strategy.

VII Conclusion

This chapter is split into four parts, the first being the mutual conclusion and the comparison drawn from the two studied cases. The aim of this section is to draw on the differences between the cases as well as the factors that are mutual for both cases. The second part discusses the implications that this research will have for the Icelandic fish industry and the third part highlights the theoretical implications of this research. Finally, suggestions for further research are discussed in the fourth part.

VII.1 Mutual Conclusion and Comparison.

In this chapter a conclusion is drawn from the two cases of UIFP and IFPC as well as looking at how these cases have contributed to finding an answer to the research question on which this thesis is based. A comparison will also be made between the two cases in order to put forward a general implication from the study.

The research question that was put forward is *“What is the role of the “central firm” in strategic alliances involving large numbers of small and medium size enterprises?”*

- a) What is the role of the central firm in the governance (administrative mechanism/coordination/management) of the alliances?*
- b) What methods have been used to coordinate activities and actors in the alliances as a whole?*
- c) How has the structure of the alliances changed over the operation time and what has influenced these changes?”*

Other topics or themes also emerged in the analysis of the cases but these questions will be used as guidance in drawing the mutual conclusion of the two cases.

VII.1.1 Form and Structure of the Alliances

In order to start this discussion it is helpful to look at the last part of the research question that is the structure of the alliances. Both alliances have moved from being joint ventures between producers to being independent

Limited Liability Companies and in the case of UIFP in minority ownership of producers. It is interesting to see that during most of the operational time of these two joint ventures the “child” had a dominant status in the relationship with its “parents”, that is the producers. This inversion of the status in the joint venture can be traced to factors such as increased *independence* of the child, the *position* of the child as a *central firm* in the value chain, *large numbers* of parents, the *small* size of the parents’ companies and *equality* between the parents.

Independence was granted to the child in both cases when they, in their early days, were suffering from a lack of freedom from their parents. This increased freedom made it possible for the child to build up own capital as well as gaining increased freedom in financial matters. Also the child achieved increased freedom and independence in governing its own matters without parental interference on day-to-day basis. Due to this increased freedom and independence and the position of the child as a central firm in the value chain dominant stances against its members, that is producers were quickly built up. The child achieved the dominant status by nature of this central position. Hence, the central firm took control of one of the most important features of the network, that is the flow of information and therefore the flow of knowledge and learning in the network. The analysis of the two cases undertaken in chapter VI showed that the central firm blocked this flow of information both consciously and unconsciously, which gave the central firm dominant position over its producers. Another factor that affects this and made the status of the child stronger is the high number of parents in the network. In addition to the high number of parents, the rather small size and equalisation made it almost impossible for individual parents or blocks of them to dominate the child. This was the essence of both networks, that is, no members could dominate the alliances for their own benefit. The downfall of this system is that the child is almost without ownership. This cause a lack of strategic leadership in the network whereas the child, in a dominating position in the network but not holding a defined role of leadership in the network, has grown and developed on more or less an ad hoc bases depending on the environment and its own interest each

time. The result of this lack of ownership and leadership in the network will be discussed in more detail later in this concluding chapter.

It is clear from the analysis undertaken in chapter VI that both the business environment in the fishing industry and the economic environment have had great impact on the development of the networks. Before the ownership change, both networks were built on enforcement. This can be traced to the monopoly of UIFP and the duopoly of IFPC and IS on selling fish products to the US. These export barriers formed exit barriers inside the fishing industry where producers were almost in a position of not being able to leave the marketing organisation due to export barriers. Hence, the marketing companies never had to face any really serious competition for the producers' business from other marketing companies. The analysis of the two cases showed that competition is entering more and more into the relationship as well as into the fishing industry as a whole. The analysis revealed that many of the new generations of managers both in the marketing companies and production companies, tended to view the environment as completely competitive, believing that competition would solve all their problems. One aspect of this increased competition in marketing the fish products is the increased concentration in the fishing and processing sectors that has occurred in the past few years. This concentration can mainly be traced to increased access to capital through improved admittance of the companies to the stock markets and the ITQ system that allows the companies to buy out or merge with other companies in the fishing sector. Despite this view, it is clear that the marketing companies built their competitive stance in the markets not least on cooperation and a good relationship with the producers.

Another view of the environment surrounding the two networks is that pressure from the stakeholders has highly influenced the development of the two networks. Before 1990, these stakeholders were mainly the producers and the government through its involvement in controlling the economic environments in Iceland as described in chapter III.5. After the ownership changes of the two networks, the shareholders took over as the most influential stakeholders. The impact of shareholders became obvious in the

IFPC case of the annual meeting for the year 1998 when one producer “bought” himself the seat of Chairman of the Board. Producers still own a majority share in IFPC in 1999 but in the UIFP case the producers own just around 20% of the total share in the company making it obvious that others beside producers are becoming the most influential stakeholders. Another example of external influence on the structure of the industry is the fisheries management system that is controlled by the parliament. By allowing the quotas to be moved between fishing vessels, the structure of the industry has changed through increased concentration in the fishing and processing sectors. The government can clearly control the development in the fishing industry through the fisheries management system, which can have a great impact on the structure of the industry and the network. Hence, the impact on the networks of external stakeholders, such as the government and the shareholders suggests that it is necessary to add environmental factors, such as stakeholders’ impact to the analysis of networks. It is claimed here that bringing the stakeholders impact into the analysis would bring more depth into the network perspective as Hakansson and Johanson¹ have put forward.

At the same time as the environment is getting more and more mixed by being both competitive and cooperative it is clear that the increased competition in the networks has accelerated changes in their structure and nature. Before the ownership change, both networks were conservative and slow to react to changes in the environment. Competition and freedom have acted as driving forces for change to the network and, in the case of IFPC, made it more flexible towards the needs of individual producers. Also concentration amongst the producers has increased their demand for service from the marketing companies. In the same way, this concentration has made the producers better capable of taking on more complicated and demanding tasks than before. This flexibility does not have as high a priority in UIFP due to the homogeneous products that they are buying from their producers. It is, however clear that after the ownership changes the relationship between the marketing companies and the producers is much

¹ Hakansson, H. & Johanson, J., 1992.

more clearly defined and producers should know much better what to expect.

In the joint venture, the interface between each producer and the marketing company was more or less the same, meaning that all producers had access to the same service on an equal basis. After the ownership change, the nature of the alliances changed from being a joint venture between producers into individual alliances between the marketing companies and each individual producer. Therefore, the nature of the alliances became more complicated due to the different aims of each producer which the network has to meet. Due to this, as well as the influence of the environment on the network, it is concluded that to view the relationship after the ownership changes, the network perspective is necessary. The network perspective views the relationship between companies in the alliances in a more holistic way than just studying individual alliances between actors in the network². Each producer contributes to the network by, for example, broadening the scope of the products, which are for sale, as well as maintaining the economy of scale of the network. Vice versa, each producer benefits from the contribution of other producers to the network by keeping it effective and economical. This supports the view that network should be studied as a whole instead of individual business relationships between producers and the marketing companies. Hence, the use of network perspective offers good guidelines to the study of the two networks.

It is clear from these two cases that the lack of freedom and competition in the network has made it conservative and stagnant. The lack of ownership has also supported this development towards stagnation whereas the network has lacked the clear strategy and authority that clear ownership is more likely to provide. It can therefore be concluded that in networks as UIFP and IFPC, the freedom to leave the network and the constant evaluation of all options that follow competition are vital for networks, as this is the driving force for changes. In the same way, clear ownership and authority is essential to move the changes forward. Lundgren points out that mutual learning adjustment and learning are the driving forces for changes

² See for example Axelsson, B.; Hakansson, H. & Johanson, J., 1992.

in a network³ but the conclusion here is that the precondition for that to happen, *is that the network is operating in competition, with the freedom to leave and clear ownership or leadership.*

VII.1.2 Governance of the Alliances

The mechanisms of governance for both UIFP and IPFC have been based on centralisation of coordinating activities and the information flow. In the IFPC case, it is clear that two mechanisms exist, a) the formal mechanism⁴ based on centralisation and rules and b) the informal mechanism⁵ that builds on direct communication and personal contact between actors in the network. This is not as clear in the UIFP case where the formal mechanism built on centralisation has more or less been maintained. There was no clear indication that either producers or UIFP subsidiaries have tried to avoid this formal mechanism and centralisation. Despite this formal mechanism of UIFP, personal contacts and mutual adjustment of the individual companies in the network were used to maintain the mechanism and to solve problems that arose in the network on an ad-hoc basis. However this mutual adjustment was exercised much more in the IFPC network due to more complicated products and marketing conditions.

It emerged from the research findings in chapter VI that both these companies used centralisation in order to gain and maintain power in the value chain. This reflects Pfeffer's view that power can arise from centralisation of control and activities⁶. This is obvious in the case of IFPC due to a lack of authority over its subsidiaries and producers. In the UIFP it is rather the nature of the business, homogeneous products, few buyers and a high number of small producers that justify this centralisation. It has to be considered when generalising from this that it is not until after 1985-90 that the business environment in Iceland and the economy, the size of the

³ Lundgren, A.

⁴ Formal mechanism is defined here the administrative mechanism based on rules, centralisation, communication through the hierarchy of the companies but not direct and description on how things should be done.

⁵ Informal mechanism is based on direct communication, decentralisation, mutual adjustment, and personal relationship and on ad-hoc basis.

⁶ Pfeffer, J., 1992.

producers and producers' capability, made it possible for them to take on more responsibility and therefore push for changes to this centralisation. Until 1985-90 participant companies in both networks seemed to have accepted this centralisation as an economical way of achieving the coordination.

Due to the centralisation of the mechanism in both cases, the mechanism is characterised by the methods of a vertically integrated firm. Johnston and Lawrence describe this characteristic well when they say that large vertically integrated companies tend to share as little knowledge as possible as well as, in many cases, viewing their external relationship in accordance with the dominant competitive perspective, concentrating on maintaining bargaining power over their divisions and subsidiaries⁷. In addition to this, the bureaucratic structure results in the managers' lack of knowledge about activities along the value adding chain⁸. Although Johnston and Lawrence describe large vertically integrated firms, the description is transferable to the mechanism of the two cases. The tendency to share as little knowledge as possible is especially true for IFPC before 1986 and UIFP for more or less all its period of operation. The dominant stance of the central firm is also in accordance to this description. The small amount of knowledge sharing was in both cases, due to blocking of communication between these sectors. Bjarnason supports these results in his research on export behaviour in the Icelandic fish industry which revealed that inadequate communication between producers and the marketing organisation has impelled producers to go into direct export themselves. Bjarnason claims, *"Further involvement of the PIE-1⁹ firms in exporting was provoked by factors such as increased marketing orientation and enthusiasm among managers in these firms, too much product specialisation of the Principal EMCs¹⁰, inadequate level of communication between the PIE-1 Firms and*

⁷ Johnston, R. & Lawrence, R. P.

⁸ Johnston, R. & Lawrence, R. P.

⁹ PIE-1 stands for Partially Integrated Exporters-I. They are key members and principal owners of marketing organisations as UIFP and IFPC and sell all their frozen and salted products through those companies.

¹⁰ Principal EMCs stands for Principal export management companies, which includes both UIFP and IFPC.

*the Principal EMCs, and a failure by the Principal EMCs to respond to some structural changes within the fishing industry.*¹¹” Bjarnason is here referring to how slow the big marketing companies such as IFPC, UIFP and IS, have been to respond to changes.

Concerning the governance of the network the question as to whether to support centralisation or not became one of the main issues. With increased size and capability of the producers they have made more demands on being responsible for their marketing operation and are less grateful for the interference of the central firm into day-to-day activities. This became much clearer in the IFPC case where the producers as well as the marketing subsidiaries showed signs of desiring to avoid the centralisation that was exercised in the network. In this matter there is difference between these two cases. First of all, after 1990 IFPC, the central firm had no core activities in the value chain after the sale was transferred to the marketing subsidiaries¹². UIFP has always had some core activities in the central firm and put less emphasis on transferring them to the markets. The homogeneous products of UIFP also help in maintaining the centralisation. After IFPC transferred its sales to the markets, other participants have increasingly started to view them as a cost in the process much rather than having value adding impact. The development of IFPC, that is to transfer the activities to participants’ companies, reflects Lorenzoni and Baden-Fuller’s view when they claim that successful central firms tend to stick to very few core skills and assets and hand out as much as possible of the resources, making the alliances as much as value adding for the participating companies as possible¹³. On the other hand, the case of UIFP is much more in the direction of the vertically integrated firm where the main emphasis is on their own value creation instead of the participants’ companies.

One of the issues concerning the governance mechanism is that in the IFPC case, the central firm suffered from a lack of defined role in the process after

¹¹ Bjarnason, A., page 325.

¹² See discussion in chapter VI.1.2.1.2 and VI.2.2.1.2.

¹³ Lorenzoni, G. & Baden-Fuller, C.

they moved the core activities to the marketing subsidiaries, while the UIFP had a defined role in taking care of core activities, as for example sales. This indicated the need for the central firm to have some defined role in the process. According to the research, two ways to approach this emerged. The first is to have some core activities, as in the case of UIFP, through selling to some markets and taking care of all purchases of products in Iceland. Hence, the central firm is seen as having some role in the process as well as making the perceptibility of the transaction and value creation difficult. The other approach is to leave the process, as IFPC is planning to do (in 1999). The precondition for the central firm to leave the process is that they obtain the necessary authority to place them selves in a strategically leading position in the process where they have a defined role of leading the network and creating the environment for participants' companies. Thus the central firm becomes what is called in the literature as a "strategic centre"¹⁴. Lorenzoni and Baden-Fuller claim that the essence of successful strategic alliance is the need for the network to have strategic leadership in form of a "central firm"¹⁵. They take an example from the Italian textile industry (Benetton) of a vertical network in the value adding chain. The two cases taken here are both of a vertical network in the value adding chain, so the similarity is clear. The two cases support the need for a strategic centre in a network that is responsible for creating environment for participants' companies and to implement changes that are needed to maintain the network. This is supported by the fact that both of these networks have lacked clear leadership and ownership making the network conservative and slow to respond to changes in the environment. This supports Lorenzoni and Baden-Fuller when they say that without strategic leadership the network becomes unable to meet the challenges of today's markets¹⁶.

The need for strategic leadership in the networks raises questions on methods of governing networks. Three main forms of governance can be

¹⁴ Lorenzoni, G. & Baden-Fuller, C.

¹⁵ Lorenzoni, G. & Baden-Fuller, C.

¹⁶ Lorenzoni, G. & Baden-Fuller, C.

analysed for the literature and the two cases taken in this research. In the network perspective the emphasis is put on almost “grassroots” movements where the driving force for change can be traced to direct communication and mutual adjustment amongst the participants’ companies¹⁷. On the other hand the theory behind the strategic centre puts emphasis on the need for someone in the network to be responsible for leading the network, which has been, defined here as informal mechanism¹⁸. The third method of a vertically integrated firm emerged from the analysis of the two cases where the governance is highly characterised by centralisation defined here as the formal mechanism. It is claimed here that the centralisation in the network and the clear separation of activities that occurs between the production and marketing sectors have damaged the possibility of value creation for the producers. Centralisation has acted as a barricade to the transfer of knowledge between these two sectors by blocking direct communication and information flow. This has also created and maintained two different cultures in the two sectors built on clear cut activities between these two sectors and the interference of the central firm.

The research showed that there is a need for the mixture of formal and informal mechanisms of governing marketing networks as in these two cases. Due to the high number of participants’ companies, and often their small size the formal mechanism and centralisation is in many ways more economical than the informal mechanism built on direct communication between all actors in the network. This is especially valid when the products are standardised and under the brand name of the marketing companies. Then it is much more economical to centralise the buying or selling of those products instead of having sales people in the markets contacting all the producers and even competing with each other for the products. On the other hand, in value added products and more specialised products direct communication and overview of all steps in the value chain is necessary. In a similar way it emerged from the research that the informal mechanism with direct communication and overview over the value chain is

¹⁷ See for example Axelsson, B.; Hakansson, H. & Johanson, J.; Alter, C & Hage, J.

¹⁸ See for example Lorenzoni, G. & Baden-Fuller, C; Jarillo, C. J.; Grandori, A.

much more likely to be value creating than the formal mechanism that often blocks the route for direct communication and contacts. It is therefore concluded that this marketing network with a high number of participants' companies needs to support a mixture of mechanisms to govern the network; the formal to make it economical and the informal to create value for the participants' companies.

VII.1.3 Role of the Central Firm

Before the ownership changes, both UIFP and IFPC defined their role against their producers to be “Service Company” or “Service Unit” for them. Hence, during most of the period of operation the two companies focused on serving the producers' need by selling their products. This resulted in the network being driven by the products of its members. An example of this is explicit in the interviews where almost all of the interlocutors never talked about marketing of products, only about selling products. Interlocutors claimed that this was due to the nature of the network selling their products as well as the lack of authority of the central firm as a previously quoted statement from a manager inside IFPC in chapter VI.2 indicates.

“It is difficult to see how we could be a leading force and also have some political influence because we are just a service unit in the ownership of the companies that we should have political influence on.”¹⁹

This is especially true in the case of IFPC. After the ownership change both companies have redefined their roles and the definition of UIFP is to be an “*international marketing and production company in chilled fish production*”²⁰ and for IFPC it is “*a global sales and marketing company for frozen fish products.*”²¹ In the case of UIFP it is clear that soon after the ownership changes UIFP changed its strategy and the role of the central firm. Now it was not meant to be a service unit but a freestanding marketing company and later on a production company as well. This has become explicit in the way that UIFP has become a vertically integrated

¹⁹ Interview with manager of IFPC, I-3.

²⁰ Taken from UIFP strategy on the www.sif.is.

company and in a sense this is in competition with its producers in Iceland. IFPC started later in this development and it is not until 1999 that IFPC is moving from being more or less a service unit towards a more freestanding business unit responsible for creating and leading its network.

What can be learned from the history of these two cases is that there is definitely a need for some leading company in the network. Before the ownership change of UIFP and IFPC, the central firm had all the potential to do that, but lacked the authority to lead the network. In addition, it has not been recognised or defined by the participants' companies that the central firm should have the role of leading the network. From the literature analysis it emerged that the role of the central firm in the network should be twofold, first, to strategically lead the network and second, to create the environment in which the participants' company should work. What emerged from the two cases is that the two networks have lacked this leadership and failed to create the environment. Therefore it can be concluded *that in order for networks or strategic alliances with a large numbers of participants' companies, to become successful they need to be led and governed by a strategic centre, which has the necessary authority to implement changes to make the alliances competitive on the markets and effective for the participants' companies.* As was pointed out in the literature analyses it is often unclear what factors should be included in this environment which the central firm is meant to be responsible for creating. A lesson can be drawn from the two cases. The main factor, which should be prevalent in the environment, is the flexibility to meet individual demands of participants' companies and value creation in the network, that is, how encouraging the environment is for the participants' companies to increase their value creation.

It emerged that the two cases did not have the same needs regarding the networks' environment. Producers in UIFP had much less need for flexible environment than IFPC. This is due to the homogeneous products of UIFP. It was interesting that in interviews with producers standing outside UIFP much was talked about the lack of flexibility and the possibility of achieving

²¹ Taken from IFPC website <http://www.icelandic.is/>.

their own strategy. This was given as an explanation as to why they did not stay in the business of UIFP. On the other hand, in IFPC there was definitely a need for a flexible network, whereas producers required direct communication with their customers. But they also had standardised products that they were happy to get rid of as soon as possible and without any specific knowledge of who bought them. Hence, it can be concluded that the processing stage of the products determines the needs for direct communication and the degree of flexibility required by the network or in other words, *“standardised products and/or low value added products demands little flexibility²² meanwhile special products and/or high value added products call for much more flexible environment with direct communication and overview of all the value chain”*.

Another aspect of the environment is the value creation, which from the research analysis emerged as the single most important factor in the network. The same can be said about the demands on value creation as was said referring to flexibility; that is, the process stage affects the demands. Low value added (less processed) and/or standardised products demand not much of value creation and vice versa. Two forms of value creation emerged in the analysis undertaken in chapter VI. In the UIFP network the emphasis on the value creation is entirely on value creation inside UIFP itself instead of what of the producers. The producers get value creation more effectively through the system of UIFP and in the form of higher prices, less stocking time and quicker payment. UIFP is not focusing on value adding in the form of further or secondary processing, by its producers but rather on secondary production inside their own constellation. On the other hand, IFPC needs to think of the value creation of its producers in the form of further processing. For the majority of producers inside IFPC, the possibility of increasing their value creation is essential. Affecting this is the conflict of interest in the network where IFPC itself, through its subsidiaries, is in secondary processing, causing certain competition and conflict with its producers. It emerged from the analysis in chapter VI that

²² A flexible environment for participants' companies means the ability of the network to meet the different needs of the participant companies.

this conflict has delayed the development of further processing in the processing sector in Iceland. This is due to a lack of information from the markets to the producers, which has blocked transfer of knowledge between these two sectors. This has affected the ability of the network to learn and adapt to market conditions. Learning and knowledge that the marketing subsidiaries acquire have not been returned to producers. The explanation for the blocking of information from the markets to the producers is twofold. The first was the previously described centralisation of information flow by the central firm traced to a lack of authority and a defined role in the value chain. This was discussed earlier in this concluding chapter. The second explanation is the conflict of interest that occurs when the marketing subsidiaries, which are responsible for returning the information from the markets, are in secondary processing as well. Participants in the research were more or less unanimous. It has to be recognised that managers are human and if they are in a situation of conflicting interests will think of their own interest before they think of others' needs, especially when the profitability of their companies may be damaged. Hence, managers of subsidiaries that are both operating a marketing office and a secondary processing plant are in position where interests conflict with the producers. As a result, they will think first of the subsidiaries' needs. The research findings suggest that it is unlikely that these managers will return information to producers in a way it will encourage them to go into further processing in competition with the subsidiary.

It is concluded in this research that one of the *“major roles of the central firm is to create an environment that is value creating for the participants' companies. The precondition for value creation is to avoid a conflict of interests between actors in the value chain and to establish the uninterrupted transfer of information and knowledge between actors and levels in the value chain”*. This means direct communication that will support and stimulate producers to become value creative where they will have an overview of the whole value chain. Direct communication supports both better marketing knowledge by producers and better knowledge and

understanding by the marketing sector of the needs and aims of the producers. The paradox here is that this is relevant to special products, but in standardised products certain centralisation can return better value creation for the participants' companies through a more economical and effective system than direct communication between all actors in the network. By this the network will have to move from being product driven to become a knowledge and information driven network where the emphasis is not just on migrated knowledge but rather embedded knowledge that builds up learning inside the participants' companies. This supports the increased emphasis in the literature about learning and the importance of knowledge transfer in the network²³. The research shows that the precondition for this is an environment which is flexible and has eliminated conflict of interest between participants' companies.

To sum up the conclusion, it is clear that the governance of networks and strategic alliances does not fall under the visible hand of the hierarchy or vertically integrated firm or the invisible hand of the free markets. In the same way it is difficult to locate the two networks in between the two extremes of hierarchy and markets. Much rather a third dimension is needed in this picture of hierarchy and markets, where the rationalisation of the network is based on cooperation, i.e. a win-win strategy that supports the use of Quchi's model²⁴ described earlier in chapter V.2 and figure V.4. Despite this, the research shows that freedom²⁵ and certain competition is essential for the network to push for evaluation on the performance of the network thus creating a driving force for changes to the network's structure and operation. In the same way, clear ownership and/or leadership is necessary to implement these changes. In a network where ownership is not clear or equality is an important factor it is essential that some companies or actors have the defined role to govern and lead the network and are supported with sufficient authority. The most suitable candidate to govern and lead the network is the central firm. Whether it is directly participating

²³ See for example Badaracco, J. L. Jr.

²⁴ Jarillo, C. J.

²⁵ Freedom is defined here as the freedom for producers to evaluate and choose the way of marketing their products.

in the value chain or plays only a governance and leadership role in the process does not matter. Hence it is essential that a network with a high number of participants' companies is governed and led by actors that have the defined role and authority to do so. According to these findings this role of the leading company should include the role of governance of the network as well as that of a strategic leader creating and maintaining the network environment.

VII.2 Theoretical Implications

This research contributes to the literature in three main fields. Firstly, the research contributes to literature in the networking of small firms, especially networks with a high number of participants' companies. Secondly, this research identifies important factors of governing network such as the need for ownership and the fact that some companies have the defined role of governing and leading the network. Thirdly, the research findings contribute to the network perspective and a better understanding of it, especially the importance of environmental factors relating to the development of the networks.

The research findings have an implication on the limited literature about networking for small firms with a high number of participants' companies. The conclusion of this research strongly indicates the need for a network to be led and governed by a responsible company. The findings suggest that due to the high number of participants' companies, the network can be in a situation where it lacks ownership. This emerged where equalisation between participants' companies was the aim and where no company had the responsibility to lead and govern the network. This indicated a difference from most of the literature relating to network and strategic alliances²⁶ where the emphasis is rather on the danger created where companies in the network are trying to dominate its governance and strategy, thus damaging the network. The findings support Doz where he claims that the "operating interface between the two partners cannot be left

²⁶ See for example Harrigan, R. K., 1985 and 1988.

to change and to ad hoc adjustment.²⁷“ This research reveals that this is the same for networks with a high number of participants’ companies, i.e. the governance cannot be left to some ad hoc changes and adjustment. Hence, the network needs both formal and informal mechanisms to make the governance effective and competitive.

This brings the discussion towards the governance of the network. The literature about the governance of a network or the nature of that governance has in many ways been unclear. The literature about strategic alliances and networks is often characterised by a discussion of the relationship between two or a few companies, as a previous quotation from Doz shows²⁸. In addition, the network perspective places a strong emphasis on such informal mechanisms as mutual adjustment and personal contacts in coordinating activities²⁹. Furthermore, the research findings indicate that a formal mechanism is necessary in governing the network as well as having a company in the network that is responsible for leading and governing the network. This supports literature that points out the need for strategic leadership that has been defined as “centre”³⁰, “hub firm”³¹ or “focal firm”³². At the same time, the research findings support the need for the informal mechanism to govern the network and to build up trust that supports the managers of participants’ companies to meet each other’s needs by mutual adjustment.

The findings of this research indicate that it is freedom and competition which are the driving forces for changes in the network. This emerged in cases where there was no company in the group researched that was responsible for changing the network or had the necessary authority to do so. Therefore it is clear that a network with a high number of participants’ companies need to be governed and led by a central or focal firm that has the responsibility and authority to do so. It is therefore concluded that

²⁷ Doz, L. Y.

²⁸ Doz, L. Y.

²⁹ Lundgren, A.

³⁰ Lorenzoni, G. & Baden-Fuller, C.

³¹ Jarillo, C. J.

³² Easton, G.; Built on Mattsson, 1986

without this the network will stagnate and become too slow in responding to changes in the environment.

The role of the central firm can, however, never be the same as with the headquarters of vertically integrated companies where the authority is much clearer. According to the findings, the role of the central firm should rather be to create the environment and lead the strategy of the network. This supports Lorenzoni and Baden-Fuller where they claim that the rule of the central firm is to create an atmosphere rather than just coordinate and rule the network³³. The research findings also support Lorenzoni and Baden-Fuller where they claim that the two most important factors of this environment are flexibility of the participants' companies to meet their own strategic goal and the possibility for value creation³⁴. In the value creation, a conflict of interest between the central firm and other participants pinpoint the danger of internal conflict in the network that can block information flow and therefore the learning process of the participants' companies. Therefore the research contributes to the literature by pointing out how an internal conflict in the network can undermine the possibility of participants' companies becoming value creative, by leading to too much centralisation and blocking of direct communication. An example of this is taken in chapters VI.1.2. and VI.2.2 where in the UIFP the lack of information from the markets has caused the failure of the grading system to reflect the markets thus causing lower value adding in Iceland. A similar example is taken from IFPC where the conflict between the secondary processing of IFPC and primary processing by producers have resulted in information from the markets not being returned to the producers.

The research findings shed new light on the need for clear governance in the network where a mixture of formal and informal mechanisms is used. The formal mechanism is to bring in the necessary effectiveness and the informal to create flexibility and value for participants' companies. It also revealed the danger of placing too much emphasis on the formal mechanism and centralisation which could block the flow of information and knowledge

³³ Lorenzoni, G. & Baden-Fuller, C.

³⁴ Lorenzoni, G. & Baden-Fuller, C.

thus damaging learning and value creation in the network. This supports the literature on networks where the emphasis is much more on the informal mechanism or governance based on mutual adjustment and learning³⁵. Although the research findings indicate the need for an informal mechanism, it is also clear that where there are a high number of participants' companies, the formal mechanism needs to be much clearer than in a relationship with only two companies. It is difficult to find a balance between the economic need of the formal mechanism and the need for creativity and flexibility of the informal mechanism. One of the most important elements that influence the balance between the formal mechanism of centralisation and informal mechanism of decentralisation is the processing stage of the products. Hence, for standardised and less value creative products, centralisation is a more effective and economical way of coordinating activities. Therefore, in a centralised formal mechanism the value creation for participants' companies is mainly through the effectiveness and low cost of selling the products. On the other hand as the processing stage and value creation increase, the demands for decentralisation get higher. The research findings indicate that "*the informal mechanism with decentralisation and direct communication was much more likely to create value for the participants' companies*".

Finally, the research implications are concerned with the network perspective that is increasingly quoted in the academic literature relating to cooperation between companies. The development of the two cases supports Devanna and Thichy where they claim that strategic alliances are getting more informal and more specific in scope³⁶. It emerged that as the marketing companies became more independent, the relationship with the producers loosened up. In the case of UIFP this became evident where UIFP do not have a contract with their producers. The relationship is based rather on trust between the companies. This development, on the other hand, indicates the need to view the relationship as a network with individual strategic alliances between the marketing companies and each

³⁵ See for example Lundgren, A.

³⁶ Devanna, A. M. & Thichy, N.

producer. These strategic alliances could then differ depending on the need and scope of the business that is included in the relationship. This research supports the need for the network perspective and with a history over fifty years these two networks show that obviously an organisational-form of network can be as competitive as much of a go-it-alone strategy, especially for small companies.

In the two cases studied, the business environment had a great impact on the form, structure and operation of the network. Included in this business environment are governmental decisions and the economic environment in which the network is operating. With increased freedom in the Icelandic economy this has changed. Now it is rather the shareholders that put on the pressure for different approaches to the operation where profitability is the single most important factor. These external or environmental factors could be phrased as stakeholders' pressure. The impact of this kind of pressure on the network suggests that it has to be taken into consideration in analysing networks. This suggests a need for broadening the basic network perspective that Hakansson and Johanson put forward and consists of actors, activities and resource³⁷. The analysis suggests that stakeholders' impact should be recognised and including in the analysis as presented in figure VII.1.

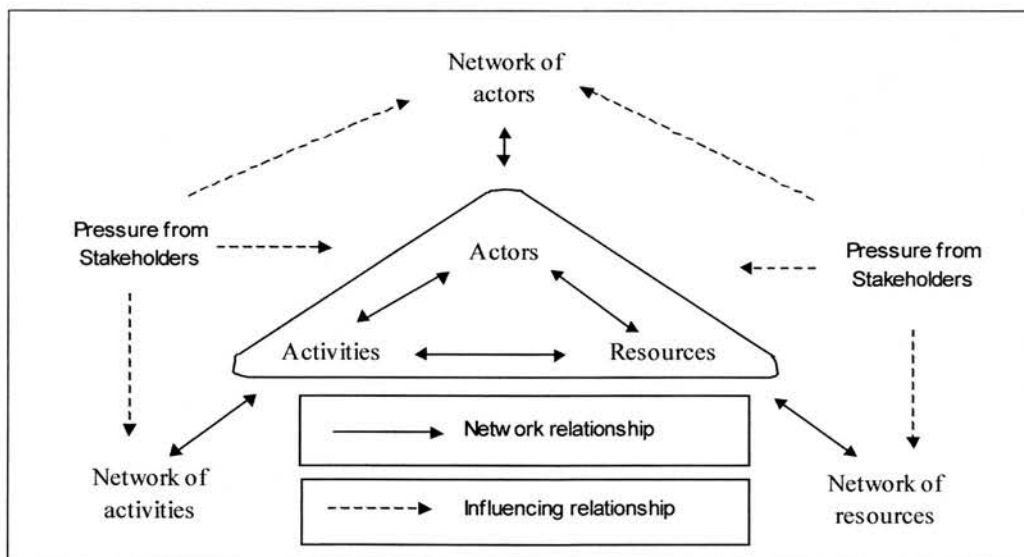


Figure VII.1 Network perspective

³⁷ Hakansson, H. & Johanson, J., 1992.

Another option is to regard the stakeholders as actors in the network. It is clear that the impact of the stakeholders can differ between networks. In the Icelandic economy, the impact of the export of fish products is considerable and the two cases chosen here play an important role in that export. It is not strange therefore that the government and other stakeholders have tried to influence the way they have developed. An example of external influence in the networks can be seen from this research where the fisheries management system, that is the quota system, has a clear influence on the actors and resources in the network. Hence, government can have a major role as a stakeholder and put external pressure on the network. The findings support the need to consider the environment in which the companies are working and its impact on the companies and the network instead of viewing the company as a completely freestanding unit not being influenced by its environment³⁸.

VII.3 Implications for the Icelandic Fish Industry

The Icelandic fish industry has in the recent years gone through massive changes where the production companies are getting bigger and more capable of taking on the increased competition. Changes have also been experienced in the export sector where the companies are entering the stock market and merging. These changes can be traced back to alternations in the Icelandic business environment, where companies are increasingly entering the public stock markets and freedom is increasing in the Icelandic economy. Changes in fisheries management, especially the ITQ system, have also made it easier for companies to buy out other companies and transfer their quotas to their own fishing vessels. These changes, that is increased freedom in the Icelandic economy, the improved access of companies to the stock markets and changes on the ITQ system have pushed for increased concentration in the fisheries and production sectors for the past decade. Despite these changes, the production companies in the Icelandic fish industry are in almost all cases so small that it is unlikely that they will be capable of marketing their products completely through a “go-

³⁸ Axelsson, B. & Nohria, N.

it-alone” strategy. In order to do so they need to specialise more, narrow the production spectrum and market what they are selling. At the same time, it is clear that on the markets the buyers, mainly the supermarkets, are getting bigger and strengthening their bargaining position. This concentration of the supermarkets has in many cases changed their approach to suppliers. The supermarkets now want fewer of them, wishing to build up long-term relationships. Hence, it will be increasingly difficult for small companies to sell direct to the supermarkets. This makes it more difficult for small companies to compete on the markets where the buyers are looking for fewer suppliers who can serve their needs better and lower the transaction cost.

This development on the markets, with increased power and importance of supermarket chains, will in the future add to the pressure on companies within the Icelandic fish industry to work together and become part of a competitive supply/value chain instead of focusing on a go-it-alone strategy. Hence, the reality in the Icelandic fish industry is that companies will need to be able to cooperate with each other to be as competitive in the future as they have been in the past. The latest development in the export sector where the two principal marketing companies, UIFP and IS, are merging, supports the need for producers as well as exporting companies to be able to cooperate with each other through a win-win strategy. The danger is that increased freedom and bigger companies will encourage managers to gain a better competitive advantage through their bargaining power against each other rather than through cooperation. Such a development will in all cases damage the Icelandic fish industry in the long run. Rather, it is essential that these two sectors should work together in a win-win way to create an environment that benefits both. The implications of this research will help managers in both sectors to understand better the nature and demands of working in a close relationship with other companies.

It is therefore claimed that as the production companies grow and become stronger, their need for value creation will increase. Their need for taking care of their own matters such as marketing their products will increase as well. This makes great demands on the marketing companies for shaping an

environment where the producers can be creative and pursue their own strategy instead of having the central firm and the marketing subsidiaries thinking and acting for them as they have done in the past. To be able to create this kind of environment it is essential that the marketing company and the producers are not in direct conflict concerning value creation. This does not mean that the marketing company should not be in secondary processing. Rather, that the companies that are responsible for returning information and knowledge from the markets should create value for the producers and should not be in competition with the producers over value creation as the research findings in chapter VI.1 and VI.2 indicate. One of the essential factors that emerged from these research findings is that direct communication and contact between customers and producers is essential in value creation. On the other hand for a more standardised product, centralisation of activities is well justified due to the effectiveness of that system. Hence, a mixture of governance mechanisms that is formal, characterised by centralisation, and informal, characterised by direct communication, is essential to create the necessary flexibility and effectiveness for the participants' companies in the network.

Due to increased freedom for the producers in choosing their way of selling their products, barriers against leaving the marketing companies and segmentation between the companies are loosening up. Due to long time enforcement of producers to sell their products through the marketing companies it is not unlikely that they will increasingly start to export on their own to gain knowledge in the field of marketing by direct connection which has been a very limited option until now. In this atmosphere of increased freedom, it is essential for the marketing companies to reconsider what they can offer the producers and how they can create value for them that will persuade them to stay in their business. Hence, it is important that the marketing companies return the knowledge to producers and make the network marketing- and knowledge- driven instead of being an almost completely production driven network. This puts pressure on the marketing companies to reconsider their position in the value chain as well as forcing them to reconsider value creation in the value chain and their part in it. This

means that the marketing companies will have to consider whether they will concentrate on their own value creation, leaving the producers as suppliers or whether they should involve the producers in the value creation by cooperating with them rather than competing with them over the value creation.

In accordance with increased freedom in the Icelandic economy and the establishment of stock markets, it is clear that the pressure on companies in the fish industry has greatly increased. The stock markets have encouraged necessary and long overdue changes to the Icelandic fish industry, geared to making it more profitable and business-focused instead of a rather social-focused industry where the aim was often to keep up employment rather than make profit. This pressure from the stock markets has resulted in companies in the fish industry needing more than ever to be profitable and expand their operation to meet the expectations of the shareholders and the stock markets. Despite the positive influence of the stock market, it is clear that it is rather primitive, where expectation and demands are often made by people with knowledge or understanding of the nature of the business that they are analysing. This has influenced the expectations of how business should be conducted where the view of the specialist of the stock markets is often the only view that is reported in the media. The reality is that in too many cases the knowledge of the analysers of the stock markets is bound to key figures in the business and judgment is based on how they should look to please the markets. This brings with it a danger of too much generalisation, almost a “fashion”, of how business should be conducted rather than an understanding of the nature of the business. There are remarkable signs of this in the fish industry, where the marketing companies are supposed to buy all their products for resale as the stock markets claim this is the way “business should be conducted”. UIFP has in many ways set the stage for this with its good performance in past years where they have bought all their products for further sale or further production, making the producers function as their suppliers. It has to be considered that this performance of UIFP occurs in years when the prices of their products have been on the way up, causing stocking products to be profitable. This

environment, where the prices go up is not guaranteed to last as well as the homogeneous UIFP products which makes this way of doing business well justified. On the other hand, this business strategy is not likely to increase the value creation by the production sector in Iceland. Rather it supports value creation and further processing abroad. This is due to the cutting of the connection between the markets and production as well as to the fact that the marketing company is concentrating on its own value creation much rather than the producers. The research findings point out the need for a direct connection between the production and the markets to support the value creation. The networks need to be more marketing-driven rather than production-driven where information; openness and knowledge are the critical issues. The merger between UIFP and IS makes new demands on UIFP where, as the producers inside IS they are much more akin to the producers inside the IFPC network. Therefore it is not unlikely that they will put pressure on their value creation and not accept being treated as pure suppliers.

As the networks in this research have developed, there has been clear blocking of this connection causing less value creation in Iceland than would have been possible with a more marketing- and knowledge- driven network. It is important that companies in the Icelandic fish industry, both production and marketing companies, work together to create value in such a way that it will benefit both sectors. It is well justified that the marketing companies operates secondary processing abroad. But it is unacceptable that secondary processing is causing conflict with the producers, thus undermining further value creation for producers in Iceland as the research findings suggest.

As has been said earlier the production companies in the Icelandic fish industry are relatively small and they will need to rely on their ability to work with other companies and build their competitive strength on cooperation; i.e. on relationships with other companies. In the same way the marketing companies in the Icelandic fish industry will base their competitive stance on the markets on their relationships with their producers and how they can create value with them. Therefore cooperation will be one

of the biggest elements in the fish industry and the competitiveness of the industry will be based on the ability of these two sectors to work together.

VII.4 Further Research

Due to limited research in this field, this research is rather broad covering almost all aspects and history of the relationships between producers and the marketing companies in the Icelandic fish industry. This results in research, which does not go very deeply into detail in matters of relationships but rather casts light on their main factors. It points out therefore, the need for further research into more specific aspects of the network between small companies. Suggestions for further study that can be drawn from this research are therefore many, but five proposals are made.

Firstly, further research into the role of strategy and strategy formation in the network spanning a few levels in the value chain is needed. This research suggests the need for strategic leadership, which supports the literature about a strategic centre in the network. What has been studied less is the formation of strategy in such a network and even whether it is possible to build up some shared strategy in networks with a high number of participants' companies. Research could focus on preconditions for the formation of such a strategy and the impact that strategy leadership would have on the operation of the network.

The second suggestion is to study closer the value creation in marketing networks between small and medium size companies. Focus in this research would need to be on how each participant contributes to the network and the different aspects of value creation for each actor in the network. This would contribute to better understanding on the value creation in such networks, where the value creation is not as clear as in the dominant perspective and the go-it-alone strategy.

Thirdly, further research is needed into the governance aspect of a network like this. Although it is claimed that this research has contributed towards better understanding of the governance, it is limited to only two cases and much more is needed to be able to generalise on the governance of such networks. In this connection, it would be interesting to study closer what

influences the need for formal and informal governance mechanisms in networks and how different mechanisms have been used in networks.

The fourth field that is suggested here is to study the ownership of the network. It would be interesting to see more research into networks with a high number of participants' companies, where, as this research points out, the lack of leader and ownership has made the networks conservative and slow to change which contributes a danger to the competitiveness of the network as an organisational form compared to other forms.

The fifth and final suggestion is to study the effect of environmental factors on the development of the network. This would open up various options of research such as taking the stakeholders' impact on the networks and studying how they have influenced the operation, individual companies in the network and also the network in whole.

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